

AUSTRALIAN ENVIRONMENT BUSINESS NETWORK

**Submission on the
Commonwealth Government's**

Carbon Pollution Reduction Scheme Green Paper

September 2008



Sydney and Melbourne

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EXECUTIVE SUMMARY

The Australian Environment Business Network (AEBN) welcomes the opportunity to comment on the Carbon Pollution Reduction Scheme Green Paper (CPRS).

AEBN supports the government's approach in establishing a market based method to reduce Australia's emissions of greenhouse gases. Overall most of the approach taken by the Green Paper is supported. To improve the Green Paper's approach AEBN recommends:

- The Government consider international actions and especially the potential for the use of trade barriers to protect carbon leakage issues. While this is a reluctant choice, Australia may be cornered into using Border Adjustment Measures or it may find itself disadvantaged or locked out of certain markets.
- Australia be involved in the development of international energy/emissions efficiency standard for a variety of EITE industry sectors.
- Develop a definition and measurement method for carbon leakage to be used as an indicator tool.
- Carbon constrained process (where there is no off the shelf emissions reduction technology e.g. CCS) be separately recognised as requiring ongoing near complete assistance to avoid carbon leakage until such international agreements are introduced.

The submission also offers a number of recommended improvements that should aid in both the minimisation of business disruption, carbon leakage and to reach set greenhouse emissions reduction targets at minimal cost. To achieve this, AEBN recommends that the definition of Emissions Intensive Trade Exposed (EITE) industries requires change. EITEs classifications should be made broader than the Green Paper specifies. EITE industry definitions should cover both carbon permit requiring and those which do not. EITE definitions should cover first industry sectors, then later it should expand and moving on to more product specific areas.

When EITE thresholds are exceeded, industry sectors will enter into sectoral based agreements on both emissions reductions and a package of government assistance including the issuing of free permits. AEBN considers sectoral agreements to be a surgical approach consistent with most other forms of pollution control used across Australia. Use of Best Available Technology Economically Achievable (BATEA) should also be used in the formation of such agreements. Such agreements will cover most areas including reduction trajectories as well as government assistance packages which if possible include State Government assistance as well.

Sectoral agreements are considered to provide the best outcomes for the environment and to the economy. While more complex it is a necessary approach to avoid shock impact to the Australian economy for little environmental gain. Overall sectoral agreements are considered to provide the lowest emissions outcomes at the best cost.

Should the contents of this submission require further clarification, please contact Andrew Doig at AEBN on (02) 9453 3348.

RECOMMENDATIONS

- R1 AEBN recommends Australia be flexible on the controlling aspects of the CPRS to align with other OECD countries approaches to EITEs and, if necessary, this may include the use of border adjustment measures or similar trade barriers.
- R2 AEBN recommends the government engage in international discussions and negotiations to develop international energy/emissions standards for products and ensure Australian businesses receive the benefits of the development of such standards.
- R3 AEBN recommends developing a carbon leakage measurement method, possibly implemented by the Australian Bureau of Statistics, as a result of the CPRS.
- R4 AEBN recommends EITEs be defined using a low threshold to be set using the following criteria:
- For a company: threshold = 3% using CPRS cost/EBITDA + labour costs
 - For a product: threshold = 1% unit product price made in Australia (includes CPRS cost) / world product price
 - Qualifying EITE sectors or products should be organised according to international product categories
 - An appeals process be developed to consider borderline cases.

Triggering of any of the above will permit the company or product to be considered EITE.

- R5 AEBN recommends that carbon-constrained product manufacturing is recognised as needing ongoing protection from carbon pricing in Australia until effective international agreements are in place for these industries creating an emissions level playing field.
- R6 AEBN recommends that individual EITE sector/product areas agreements be developed which packages CO_{2-e} reduction trajectories with government assistance.
- R7 AEBN recommends that individual sub-permit requiring EITE sector/product areas agreements be developed which packages CO_{2-e} reduction trajectories with government assistance.

1 INTRODUCTION

AEBN welcomes the opportunity to comment on the Federal Government's comment on the *Carbon Pollution Reduction Scheme Green Paper (CPRS)*.

AEBN is an industry and business representative body specialising in environmental issues that affecting its members. Collectively its membership has a turnover in excess of \$50 billion and employs well over 50,000 people. Further information about AEBN can be found on its web site at www.aebn.com.au.

AEBN recognises the need to protect our environment and future prosperity. Climate change has the potential to not only damage the world's environment but also to directly affect business and industry adversely. Industry and business has much to lose if the environment is harmed. However, AEBN will always call for maximising the environmental benefits at minimal cost; in particular, the cost impact of regulation and reducing its burden on industry.

Many of our members recognise the need to act on reducing greenhouse emissions and have taken actions to become partially or fully carbon neutral. A number of members participate in Greenhouse Challenge programs as well as many state-based programs. Consequently, they have improved their energy efficiency and reduced their carbon footprints. Members report they are, in part, being driven by their customers to reduce their carbon intensity. It is not uncommon for customers to ask Australian suppliers for their carbon footprint.

1.1 Trading Scheme Supported – But Priorities Need Clarifying

AEBN also supports the government's use of a cap-and-trade trading scheme to provide a relatively effective regulatory method to reduce Australia's greenhouse emissions. Development of the CPRS is one of the most challenging regulatory development processes undertaken in Australia in over 10 years or more. Getting it right will be critical, both environmentally and economically. Most importantly, the CPRS must be designed to achieve specific outcomes:

- Long term outcome – to be part of a global solution to reduce greenhouse gases to minimise the impacts of climate change on the Earth.
- Short term outcome – to encourage the majority of greenhouse gas emissions countries to join in and tackle this problem together.

The Green Paper does not make it clear that the short-term priority must be to encourage other countries, by example to join in with international partners who also strongly encourage all other countries to address their greenhouse emissions.

If global cooperation to reduce greenhouse emissions fails, any reduction actions undertaken by small countries such as Australia will be futile. Demonstration that action on greenhouse emissions by developing countries is not only in their best interests, but can be achieved less painfully than perceived is paramount. To do this Australia can and should develop world best regulatory practice to establish the most efficient means to achieve a low-carbon equivalent economy. Such actions can then provide effective regulatory models for others, especially developing countries, to imitate. Australia would gain the appropriate international recognition.

1.2 Legal Structures

Forming the draft legislation for the CPRS is due by December 2008 and the actual schemes supporting legislation are due by the end of 2009. Given this timetable, AEBN recommends that the Government ensures that any laws forming the structure of the trading scheme are separate from its targets and assistances. That is any controls on how fast the CPRS reduces emissions, provides assistance and incentives are kept separate from the main Act.

AEBN is mindful there is not enough good data available for the government to accurately predict the early economic impacts of the scheme. Consequently, the 'leavers' controlling the scheme's impact on industry should be kept in a simpler legislative form to permit fast changes to its settings.

Currently there are three main settings (leavers) available to the government which include:

- 1) **Setting of the cap** – or by how much Australia's CO_{2-e} emissions are to be reduced by over time. For example a 20% reduction cap by 2020 means that emissions under the CPRS will have be reduced by 20% based on their levels at the initial commencement date in 2010. A lower cap (or even a maximum carbon price) of, for example, \$20 can be used.
- 2) **Assistance to Emissions Intensive Trade Exposed (EITE) industries** which has two parts:
 - a. Allocation of free permits to companies required to purchase permits from the CPRS. Current thinking by the Government is to allocated 20% of the funding collected by the CPRS back to EITEs. This is also been earmarked to be reduced over time to encourage further energy efficiencies from these companies.
 - b. Provide grant packages for companies that are EITEs but are not required to purchase permits.
- 3) **Defining what an EITEs is** – The CPRS has a simple draft definition. However, many EITEs under the thresholds either for needing to purchase permits or under the emissions intensive threshold are likely to be affected by the CPRS.

In tackling climate change, it is vital to the future of Australia's economy – as well as the nation's involvement with the developed world – that these settings are managed in a careful and balanced manner.

2 INTERNATIONAL COOPERATION – FIRST PRIORITY

The Garnaut Review clearly shows Australia's role in international greenhouse abatement is to make a commitment and act in common with other developed nations. It is not for Australia to take a lead, or be a laggard, in reducing its greenhouse emissions. However, Australia is in a good position to develop a lead in regulatory efficiency in managing and abating greenhouse emissions. Development of an efficient lowest cost regulatory method in overall cost will provide incentives for other countries to join and tackle this truly global problem.

Damaging Australia's economy too much by driving the CPRS with too-high reduction targets will send the wrong signal to the developing world. In contrast, doing too little will show that Australia has a mere token scheme that does not achieve significant cuts to greenhouse emissions. Hence the most difficult challenge for the Commonwealth Government is to get this balance right.

AEBN considers that cuts beyond 10–20% from Business as Usual (BAU) can only be considered a long-term objective. It can only work if most of the world's greenhouse emissions are under a similar pricing arrangement. This is a considerable challenge.

Along with other carbon-priced¹ countries, initially Australia will need to encourage carbon-lagging² developed countries to adopt a carbon-pricing scheme. The Draft Garnaut Review states:

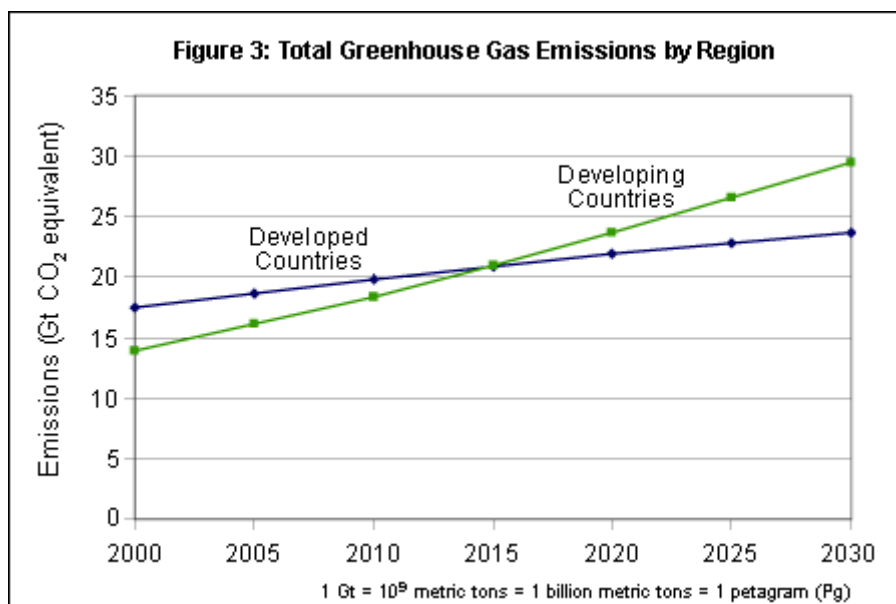
All developed countries need to be subject to, and meet, emissions reduction goals. While many will need to resort to international trading to reduce the costs of achieving deep cuts, it is important that developed countries show credible domestic abatement effort to demonstrate to developing countries not only their seriousness, but that it is possible to reduce emissions without sacrificing prosperity.

Creation of a pact of all developed countries to sell action on climate change is essential [Garnaut 11.5.3], before the developing nations are expected to join with serious carbon abatement schemes. Garnaut continues on with the theme that a comprehensive international agreement is required. Nevertheless Garnaut states that '*All developed and high-income countries, and China, need to be subject to binding emissions limits from the beginning of the new commitment period in 2013.*'

The most difficult challenge to convince the developing countries, that they should also adopt binding targets. However, without their commitment even developing countries' cuts will tend to make little difference to global greenhouse emissions and climate change. Figure 3 provides a projection of future greenhouse gas emissions of developed and developing countries. Total emissions from the developing world are expected to exceed those from the developed world by 2015.

¹ *Carbo--priced* countries means those countries which have a carbon price / reduction scheme operating or planned within 3 years.

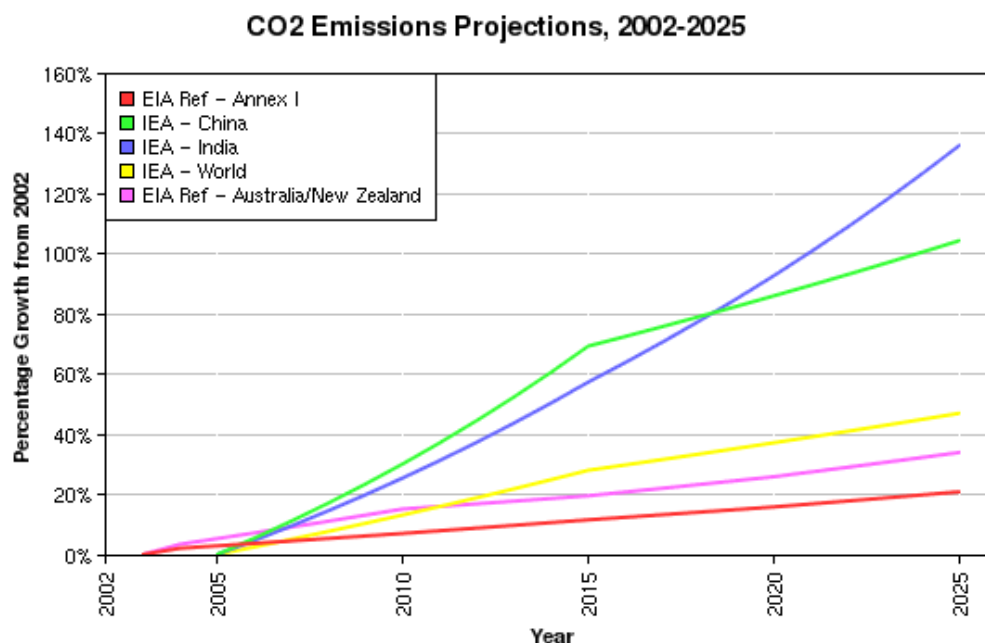
² *Carbon-lagging* countries means those countries which **do not** have a carbon price / reduction scheme operating or planned within 3 years.



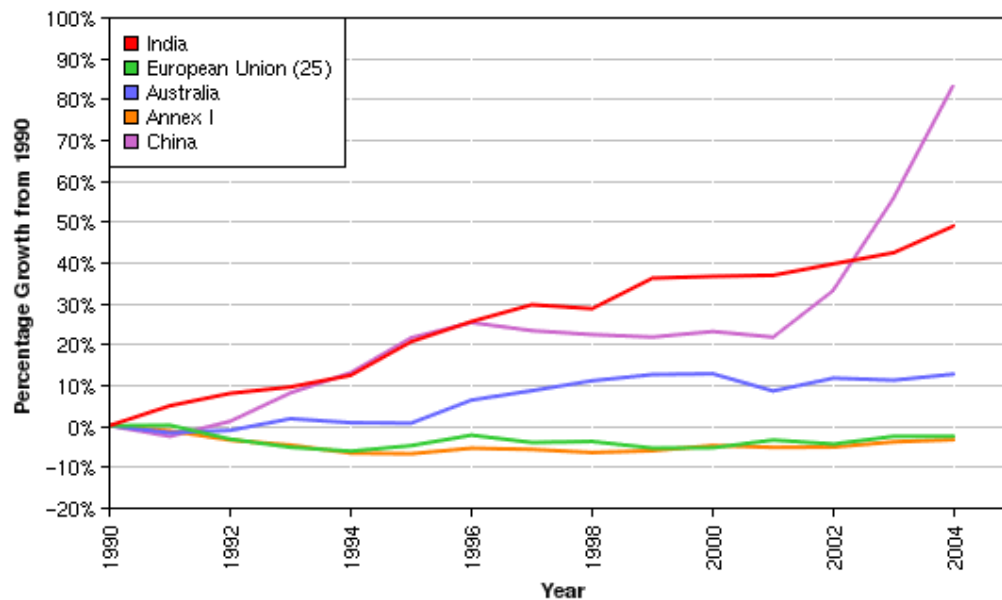
Reference: (1) SGM Energy Modeling Forum EMF-21 Projections, Energy Journal Special Issue, in press, reference case CO₂ projections.
 (2) Non-CO₂ emissions are from [EPA's Global Anthropogenic Emissions of Non-CO₂ Greenhouse Gases 1990-2020](#).

Consequently the main initial aim of the Carbon Pollution Reduction Scheme (CPRS) is to encourage developing nations to join in with the developed world before deep cuts to carbon emission can be made. The question remains as to what will convince the developing nations to adopt similar binding carbon-reduction targets that the developed countries are adopting or at least considering. Garnaut's draft supplementary report supports the contract and convergence model.

The following graphs and data were gathered from the [Climate Analysis Indicator Tool](#), from the World Resources Institute. Without the involvement of the developing countries, especially China and India, then achieving overall greenhouse reduction targets will not be possible and the world will need to brace for more severe climate change—Garnaut's *ad hoc* international outcome.



Per Capita CO2 Emissions, 1990-2004



AEBN predicts that substantial international tensions will occur well before these above scenarios come close to occurring. There is considerable talk in Australia and internationally of the use of border tariffs against products from countries without binding carbon targets or from less-efficient companies. AEBN considers border tariffs are a possibility, but internal assistance measures should be explored as a priority.

2.1 Tiers In Dealing with Carbon Leakage

Garnaut's draft report identified the carbon leakage as a truly dreadful problem. He emphasised the need to be involved in the international actions to deal with carbon leakage. AEBN proposes several approaches or hierarchies of action to deal with carbon leakage. These include, in order of priority:

- 1) *To reduce carbon leakage is to increase the number countries achieving their binding carbon reduction targets.*

This follows from AEBN's position that Australia's CPRS priority is to encourage other countries to join in and tackle climate change together. Carbon leakage will occur when there is a global imbalance between countries meeting their binding carbon emissions targets and those that are not.

- 2) *To implement import and export taxes for the international trade of CO₂-e-intensive products with non-abating countries.*

It is commonly believed that direct-trade discrimination would not be allowed under the rules of the WTO but there are precedents by the way of multilateral environmental agreements with (discriminating) trade provisions. One example is the US-Shrimp case,³ which uses the WTO

³ The US-Shrimp case – where the USA won a WTO case where companies had to use turtle excluder devices in their shrimp nets or their products were banned from import into the USA.

processes or production methods (PPMs) to ban products made in manner considered to harm the environment. This signifies use of international emissions performance standards for EITEs where the importation of a product can be banned in countries where their internal producers follow these standards.

- 3) *To protect and support EITEs industries and ply a differential approach to other industries which are not effectively trade exposed.*

By their definition, EITE industries are trade exposed. However other industry sectors are not trade exposed, such as electricity generation. However achieving a reduction target would simply shift a part of the CO_{2-e} reduction burden from the EITEs to other unexposed sectors. This should reduce leakage but would probably increase aggregate national abatement costs. There are substantial limitations to this policy approach as it would be harsh on the emissions-intensive, non-trade exposed sectors. Ultimately if this is the only approach available, then less-stringent caps and reduction targets would most likely be the outcome..

2.2 International Actions Dealing with Carbon Leakage

Carbon leakage to developing nations is being seriously considered by the European Union and starting to be considered by other countries. Below are a few examples of the EU's thoughts and proposed strategies on carbon leakage

'The Commission is committed to addressing carbon leakage. For sectors exposed to a significant risk of carbon leakage free allocation is proposed up to 100% of their share. The sectors that are concerned will be determined by June 2010⁴.

1. *The realisation of an international agreement is a first priority.*
2. *The introduction of Border Adjustment Measures(BAM) is already mentioned as an option in the EU ETS proposal. In case Europe decides to go in this direction it is of utmost importance that WTO compatibility is ensured. Furthermore, the impacts of BAM on trade and on the international negotiations must be clearly assessed. The EU ETS should provide for the right incentives towards a low carbon economy.*
3. *The concept of carbon leakage is not clearly defined and no agreement has been reached yet on how to measure carbon leakage. It is worrying that power, heat and agriculture also claim to be affected by carbon leakage.*
4. *There are difficulties concerning the gathering of data in the various industrial sectors. There is no agreement on how far sub-sectors should be taken into account.*
5. *The analysis on the risk for carbon leakage should preferably not develop into a modeling exercise. It is better to study existing data.*

'The European Council recognizes that in a global context of competitive markets, the risk of carbon leakage is a concern in certain sectors such as energy intensive industries particularly exposed to international competition that needs to be analysed and addressed urgently in the new ETS Directive so that if international negotiations fail, appropriate measures can be taken. An international agreement remains the best way of addressing this issue.'

⁴ [Report of the ad hoc meeting of the EECF working group on emissions trading on carbon leakage and auctioning](#), 11 April 2008

The EU and the USA combined represent about 56% of world's GDP. In contrast, Australia represents 1.66%. With the EU's and USA's economic might, the international carbon-abatement scene will be led. Australia will, at the international level, be a follower; however with some influence. Consequently there is no point in Australia establishing a CPRS that is out of kilter with USA–EU approaches to setting targets, and carbon-leakage avoidance measures. AEBN considers Australia will be far more bound to the actions on details on carbon abatement and carbon leakage that is considered within the Green Paper. To emphasise this point, AEBN makes the following recommendation to ensure this issue is formally addressed.

R1 AEBN recommends Australia be flexible on the controlling aspects of the CPRS to align with other OECD countries approaches to EITEs and, if necessary, this may include the use of border adjustment measures or similar trade barriers.

While the use of a 5-year cap provides certainty, there are other means by which the CPRS can be fine-tuned to deal with variations and changes to most developed nations with binding carbon targets. Typical of these is how Australia will treat its EITEs (discussed later).

The above quote also manifests the importance of carbon leakage to the EU and signals a more formal measurement process will be developed.

2.3 Tariff Barriers

As discussed in section 1.3, the EU and other countries are considering the use of trade barriers. AEBN considers that use of Border Adjustment Measures (BAM) should be only used when development of an international agreement fails. Central to such BAMs is the Product or Process Methods (PPMs), such as the WTO's US–Shrimp case.

The way such trade barriers might work is for industry sectors to first develop internationally agreed energy/emissions efficiency standards. Meeting these standards would have to be verifiable at the company level. Hence a country or a group of countries such as the EU could impose a tariff barrier that only accepts products made using a process that met the appropriate international standard. Non-conformers could have their products either banned or subject to a BAM or tariff.

To avoid being in an internationally hypocritical position, countries using such international energy efficiency standards should first ensure their internal processes are compliant. So there is an incentive for countries – and companies – to embark on the development of such standards.. The [Asia– Pacific Partnership on Clean Development and Climate](#) (APP) is developing such standards, though not necessarily for use as trade barriers but to assist developing countries to come up to speed on energy/ emissions efficiency. However, these standards or others could be used as a trade barrier over greenhouse emissions. As Australia is a member of the APP, AEBN considers we should not only be involved with the ongoing development of these standards but ensure Australian industry is involved and benefits from the flow-down of policy, technology and other effects.

R2 AEBN recommends the government engage in international discussions and negotiations to develop international energy/emissions standards for products and

ensure Australian businesses receive the benefits of the development of such standards.

3 DEALING WITH EITES REQUIRING PERMITS

3.1 Carbon Leakage – Measurement

Carbon leakage is perhaps the most difficult issue to deal with that arises from implementing the CPRS. Exporting Australian jobs, loss of business investment, loss of income from exporting industries and the possible increase in greenhouse emissions are likely outcomes if appropriate assistance and actions are not undertaken by the government.

Avoiding substantial carbon leakage should be a main component of the CPRS. The government needs to cap the level of investment reduction, job losses and economic downturn caused by carbon leakage. However there is no formal measurement method for carbon leakage. The IPCC has defined carbon leakage, but this has been criticised as being quite restrictive and it is perhaps no surprise that leakage is found to be small⁵. Indeed the definition of carbon leakage has a number of more complete definitional examples. AEBN considers such definitions and measurements of carbon leakage become an important measure for the government to use to set the ‘levers’ of the CPRS.

As discussed in section 2.2, the EU is looking to better define and measure carbon leakage. As a result, an international definition and measurement approach may be formed and Australia is then likely to use it. If Australia embraces the need to measure carbon leakage, it is then in a better position to influence an international acceptable measure of it.

AEBN appreciates that such measurements will be indicative and initial measures will lack precision. Measurement of carbon leakage is considered to face similar issues to those of EITEs. The process of measurement of carbon leakage is expected to be one of shades of grey rather than one of *this company transferred overseas because of the CPRS and therefore has 100% carbon leakage*. The question is, if a company does close, wind down or postpone expansion, how much of this commercial decision is a result of the CPRS? Overall, AEBN believes that carbon leakage can be a useful measure for fine-tuning the setting of the CPRS and use by investment processes to consider Australia’s ability to manage carbon leakage effectively.

R3 AEBN recommends developing a carbon leakage measurement method, possibly implemented by the Australian Bureau of Statistics, as a result of the CPRS.

3.2 Identification of EITEs

AEBN has had many members comment the current trajectory for carbon reduction and support for Emissions Intensive Trade Effected Industries (EITE) is too simplistic and lacking in appropriate economic data at the company level.

Use of the EITE threshold of 1,500tCO_{2-e} per \$ million of revenue suffers from a number of issues, including

⁵ Raupach, M.R. et al., *Global and regional drivers of accelerating CO₂ emissions*. Proceedings of the National Academy of Sciences, 2007. 104(24): pp. 10288–93.

- Perverse outcomes are encouraged for companies close to the thresholds – being above the carbon intensity threshold means a disincentive to be more energy efficient.
- That it is too simplistic to capture all but the most obvious areas of carbon leakage.
- Revenues are highly variable resulting in fluctuations above and below the threshold with no change in carbon emissions per unit of production.
- The sharp cut off results in harsh economic impacts on industries just below the thresholds.

The coke industry is an example where its raw material has increased over 200% in less than three years, yet its carbon intensiveness remains static. Consequently, this industry has seen its carbon intensive measure go from above 2,000 tCO₂/\$m to less than 1,000 tCO₂/\$m based on the variation of its raw material – coal.

Consequently, AEBN considers the carbon intensity of a process or company should be measured in a different manner.

In contrast to the determination of when an industry is either a EITE or not, is the method the Green Paper's uses to determine the allocation of free permits is exceptionally different and more detailed. Free permit allocation is based on process efficiency:

'Industry-wide baselines would involve developing a single baseline for each EITE activity to be applied to all entities undertaking the activity. The baseline could be either:

- *a best-practice benchmark baseline (based on Australian or world's best practice) or*
- *an Australian industry average baseline'. [The Green Paper then argues for an Australian baseline.]*

Hence the Green Paper recognises the need to consider product-manufacture efficiencies, but not at the trigger point if such an industry sector should initially be considered. Overall AEBN is concerned the approach used to identify and assess – as well as provide assistance – is too simplistic and will not generate the best value carbon-reduction outcomes. A new approach is required in which EITEs are not only more fairly identified, they are also assisted in ways to that will address their short-, medium- and long-term carbon leakage and reduction trajectories.

The Business Council of Australia suggests a cost level of between 3 and 5% from the impact of a CPRS divided by the companies EBITDA plus labour costs, this has been recommended by as an alternative, and is supported by AEBN as one method for use as a EITE gateway.

Garnaut apparently abandoned the use of the industry threshold value⁶ proposed in the Draft Report. In the Draft Supplementary Report Garnaut suggests

For every unit of production, eligible firms receive a credit against their permit obligations equivalent to the expected uplift in world product prices that would eventuate if our trading competitors had policies similar to our own.

⁶ See Page 386 Garnaut Draft Report

To AEBN there needs to be a better gateway threshold or thresholds to identify an EITE industry or even a product. This gateway should be set low, and assistance set on a much broader range. BCA's threshold is perhaps easier to access data, but Garnaut's formula is more reflective of the trade exposure. AEBN considers a combination of the 2 at least should be used. This can be done by setting a trigger for each and if one or both are exceeded, the company or product can then be described as EITE.

Also, AEBN is concerned that some companies failing to meet the threshold will also suffer undue economic hardship as a result of the CPRS. Consequently there should be an appeals mechanism used to hear special cases of merit a claim for EITE status. This can occur, for example, where some sectors have very low levels of profit margin compared to earnings. To ensure that shoulder sites are included, an appeals process needs be established to assess such borderline cases.

R4 AEBN recommends EITEs be defined using a low threshold to be set using the following criteria:

- ***For a company: threshold = 3% using CPRS cost/EBITDA + labour costs***
- ***For a product: threshold = 1% unit product price made in Australia (includes CPRS cost) / world product price***
- ***Qualifying EITE sectors or products should be organised according to international product categories***
- ***An appeals process be developed to consider borderline cases.***

Triggering of any of the above will permit the company or product to be considered EITE.

3.3 Allocation of Free Permits and Carbon Constrained Processes

Issuance of free permits to various EITE claimants is recognised as a difficult process for the government. However, to prevent excessive carbon leakage it is an essential process.

As discussed in section 1, this level of assistance should be made flexible to ensure Australia stays in line with other OECD countries. While this approach lacks specific certainty, it can provide business with some comfort that Australia will be follower of the major economic players.

Allocation using the 90% free permit use and reducing it by 6% each year is again considered too simplistic and potentially economically dangerous for many EITEs. However, AEBN supports the use of a best-practice benchmark baseline as one of the elements used to determine allocating free permits and other assistance measures.

Processes used determine the emissions-intensity of a site, not an industry sector average. In addition, international trade agreements are based around fixed tariffs, which are product specific. So to provide the fairest allocation of free permits, AEBN believes that both process and product types need to be considered.

Some processes have many off-the-shelf low-emissions technologies available, such as electricity generation. AEBN calls these carbon adaptive.

Some processes do not lend themselves to alternative low-emissions off-the-shelf technologies. AEBN calls these processes carbon constrained.

For example, the manufacture of carbon black. Carbon black is made by burning heavy oil in a reducing atmosphere followed by a rapid water quench. There is no other available technology for making carbon black in a low emissions process. Only new undeveloped technologies are a possible solution for making this a low emissions product.

Carbon-adaptive products can be set a trajectory to move to lower emissions intensive processes. Such trajectories should be predictable in price, making the trade exposures identifiable. Consequently, a combination of carbon constraint, free permits (if the company must purchase permits) and other government assistance can design a minimal carbon leakage outcome for carbon adaptive products and companies.

Carbon-constrained products can be treated in a similar fashion to carbon-adaptive products, but the exception here is the need to wait for appropriate technologies to be developed. They are more susceptible to carbon leakage as no processes exist (except in pilot or laboratory scale) to make these products in a low-emissions manner. Long term protection of carbon constrained products from the CPRS will be required. Only when an binding international agreement for a carbon constrained product has been established and implemented can the easing of assistance measures be commenced along an internationally set trajectory.

Many of the carbon constrained product manufacturers will need Carbon Capture and Storage (CCS) such as for Portland cement and basic metals. Installation of carbon capture equipment can be installed at most facilities, but a company's competitive edge will tend to come from its proximity to geological storages, as transport of CO₂ long distances will have its own costs. Perhaps a country's future competitive advantage will be its natural suitable geological storages and their proximity to existing industrial centres?

R5 AEBN recommends that carbon-constrained product manufacturing is recognised as needing ongoing protection from carbon pricing in Australia until effective international agreements are in place for these industries creating an emissions level playing field.

3.4 Individual Industry Sector/Product EITE Agreements

As discussed above, AEBN considers the environmental and economic impact of carbon leakage should be based on a more detailed surgical approach. However, to be surgical in managing EITEs industries, AEBN considers another sharper albeit more complex approach is required. Individual agreements for industry sectors based on international trade product types would generate a much more accurate method to determining emission contraction and assistance. Why does it need to also go down to the product level? Because the trade-exposed part of being an EITE requires analysis of the trade exposure.

Use of product types, while making the process more complex, appears to AEBC the best way forward if major nations commence to use border adjustment measures. Any such trade barriers will need to be addressed at the product level as tariffs are set in this manner. It will also serve to defend Australian exports if our products are challenged at borders by other countries wishing to protect their EITEs (see section 2.3).

Negotiations on the development of sector/product agreements would ensure a much fairer hearing and should, if negotiated within firm boundaries generate an effective and certain path forward. AEBC notes the Green Paper dismisses sectoral agreements as an '*inherently complex task, and invites protracted debate*'. AEBC considers that sectoral agreement will ultimately be used. The reasons for this include:

- Scale of the potential economic impacts as the CPRS cap tightens are considerable. If poorly planned and attempted in a blunt manner considerable economic shocks will occur resulting in excessive and unnecessary carbon leakage and job losses.
- Virtually all pollution control permits for large sites across Australia are undertaken via individual licence agreements and negotiations which include site-specific issues.
- All planning of new and expanded sites are undertaken on a site-by-site basis.
- The electricity power generation industry is being treated as a special case in the Green Paper and has been given in effect its own sectoral consideration.
- Improvements in the mass and concentration of emissions is largely undertaken on a site-by-site basis and process replacement basis.
- A far more efficient outcome, which combines free permit allocation, energy efficiency targets, government assistance and a clear path for industry / product area emissions per unit of production.

AEBC agrees this process is complex and can lead to delays in setting final agreements. Nevertheless, this is the way in which pollution issues are currently dealt with largely at the state level. It is not acceptable to dismiss such an important issue as too complex when all other pollutants are treated in this manner. Driving to a timetable of political implementation is also a poor reason to apply a blunt regulatory instrument to many industries. If the outcome of a blunt instrument is too brutal, then strong calls to change it should be expected.

As an example an industry sectoral agreements should:

- Include free permit allocation based on a trajectory of emissions reduction for the sector or product area – note this may result in faster reductions than the proposed plan
- Contain an emissions-reduction trajectory based on the unit of production output (and also a total mass limit where necessary) with clear timelines and that these be based on the Best Available Technology Economically Achievable (BATEA) concept⁷
- Set review periods (eg minimum 5-years) to take into account changes in caps, technologies and international actions.
- Contain renegotiation clauses where an international agreement on energy / emissions standards is prepared or modified.

⁷ BATEA has been a well established criteria used by many environmental departments to achieve effective reductions in emissions within a technical and economic window.

- Include support from the government (preferably at both state and federal levels) to assist that industry/product area to meet its trajectory.
- Be encouraged by state governments to permit fast tracking of planning approvals for new developments outlined in the sectoral agreement which meet or exceed the trajectories agreed to.

Initially sectorial agreements would involve industry sectors that are required to purchase permits. As there are about 1,000 corporations that will be needing permits then this can initially limit the initial number such agreements. However, as the price of Australian CO_{2-e} permits increase so will the impacts. Consequently the number and complexity of the sectoral agreements can be expanded to a more specific and detailed areas such as products, but this can be spread over time to enable the initial outcomes of the CPRS to be implemented and later improved upon. Improvement to the CPRS will be ongoing and will result in attending to more detailed program, perhaps ending with the details required for current environmental licences or planning approvals.

R6 AEBN recommends that individual EITE sector/product areas agreements be developed which packages CO_{2-e} reduction trajectories with government assistance.

4 DEALING WITH EITES NOT REQUIRING PERMITS

Many companies, large and small, will only see the impact of the CPRS as increased prices for energy and the flow-on effects of increased energy prices in other raw materials, goods and services.

A large number will be above the proposed threshold (see R3) of being an EITE. However, they will not be in a position to receive any free permits as they will fall under the thresholds for requiring to purchase carbon-permits. While not having to purchase permits appears to protect them from the direct costs of the CPRS, many will have to deal with the indirect costs of the CPRS.

The Green Paper proposes that compensation for these EITE industries will be provided under the Climate Change Action Fund (CCAF). The Green Paper provides a very brief overview of the issues and actions it will consider in dealing with these sub-permit EITEs.

While the recognition of such actions are welcomed the issues concerning AEBN is the allocation of funding the CCAF. The Government is apparently supporting Garnaut's position of:

- 20% for R & D
- 20% to industry EITEs
- 10% to agriculture once it is included in the CPRS
- 50% to households

This breakdown is not expressed in the Green Paper in any detail. AEBN is also cautious over the Garnaut report's choice of compensation levels, which is given as a guide, but noted that it will need further economic modelling to achieve a more detailed split.

Consequently, the lack of details on the amount of funding to the CCAF and lack of certainly to sub-permit requiring ETIEs, many industrial sites are concerned about their future under the CPRS. AEBN considers the assistance process for sub-permit companies needs to be better established and should be along similar lines to that of EITEs requiring permits. As sub-permit companies have less exposure to the CPRS, their assistance package will be proportionally less.

Assistance to the sub-permit EITEs will also be important to minimise carbon leakage. Consequently assistance packages to these industry sectors will be increasingly critical as the scope of the caps under the CPRS bite. AEBN envisages a similar scheme to assist sub-permit EITEs based on a threshold as discussed in section 3.2. If above these thresholds, individual sector/product area agreements should be developed to package emissions reduction trajectories countered with appropriate assistance packages derived from the Climate Change Action Fund and other state assistance where agreed to.

R7 *AEBN recommends that individual sub-permit requiring EITE sector/product areas agreements be developed that packages CO_{2-e} reduction trajectories with government assistance.*

5 CONCLUSION

Ensuring the priority of encouragement of the development of an international agreement on binding targets on greenhouse emissions will assist Australia's outcomes in a climate changed world.

Australia in using international developments in climate change actions will ensure the CPRS is controlled to minimise any disadvantage that may result from such developments. This will include Australia developing a measure for carbon leakage to be also considered at the international level.

The use of individual agreements for industrial sectors that trigger low-level EITE thresholds will ensure an efficient treatment of Australia's industrial areas. This will result in clear targets and timelines for our industries providing business confidence and clarity on what they will have to achieve in terms of emissions reductions. Careful balancing of trajectories with appropriate assistance measures will provide reassurances that Australian jobs will not be exported as carbon leakage and that considerable cuts will be made.

Use of Best Available Technology Economically Achievable will be used as a cornerstone in the development of such agreements. International agreements on industry sectors and or products will be included in the BATEA assessments and conditions.

Such outcomes for most industries will most likely result in faster reductions than under the current EITE assessment and assistance package.