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To

The Climate Change Group

Department of the Prime Minister and Cabinet

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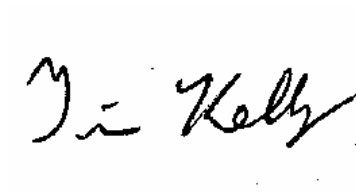
RE: Submission on the Abatement incentives prior to the commencement of the Australian Emissions Trading Scheme.

Dear Climate Change Group

Thankyou for the opportunity to comment on Abatement incentives prior to the commencement of the Australian Emissions Trading Scheme.

In this submission I have identified the potential for carbon leakage when dealing with tradeable permits and carbon credits used simultaneously with voluntary actions. The emissions trading system should be designed to discourage the over trading of benefits from uncovered sectors to covered sectors and prevent the erosion of the benefits of voluntary greenhouse reductions made by organisations should their emissions permits be sold to other emitters.

Kind regards

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Tim Kelly

Private Citizen

Residual concerns on the *Permit and Trading* approach

I have lingering concerns about the complexity, fairness and effectiveness of the proposed Australian Emissions trading scheme compared with an emissions *tax and trade* system as outlined in my [submission](#) to the Emissions Trading Taskforce. I note that I am not alone in my thinking, with the [Productivity Commission](#) also suggesting that the option of a carbon tax should be considered, and more recently, in the Committee for Economic Development of Australia (CEDA) *Getting it Right* (2007) report, Robert Shapiro for the American Consumer Institute, discusses the merits of the carbon tax as an alternative to carbon trading.

Acknowledging that the popular thrust amongst Government and business has been to praise permit and trade systems, it may still work out that the difficulty in establishing fairness in permit allocations, the difficulty of achieving permit clawback, and the complexity of the scheme may make the *permit and trade* approach un-workable. At this early stage it would be wise for economic modelling of both options to be carried out to provide the necessary foundation informed consideration of each, in case a change in the preferred option takes place.

It should be noted that if 80% of the scheme emission permits are grandfathered, the cost on carbon emissions across the entire market is only 20% of the sale price, is only acting on 20% of the liable market, and is distributed unequally and arguably unfairly.

Carbon Leakage

Carbon leakage is the basis for much of the concern in the Kyoto Framework whereby nations that are required to achieve targets can acquire Certified Emissions Reductions from developing nations such as China that are not obliged to meet targets in the first commitment period. Indeed one of the reasons that the former Howard Government would not ratify Australia's Kyoto commitment was because it felt that the Global system would be ineffective unless all nations participated in achieving targets.

There are two vulnerabilities in the proposed Australian Emissions Trading System that would replicate the very same problems of the first Kyoto commitment period into Australia's emissions trading scheme, and have an impact on abatement actions.

Vulnerability 1 Transferring the greenhouse benefits from the open sectors to the covered sectors will not reduce emissions.

The uncovered sectors of agricultural production, forestry and land use (I refer to all three of them as land based sectors) can be directly likened to China and India in the current Kyoto framework where they can sell carbon benefits whilst having no constraints on their own emissions, in this case from land based emissions. In a greenhouse sense this is potentially trading whilst insolvent, and can erode the effectiveness of the system to reduce emissions.

The Climate Group will need to determine a methodology or a market signal that suggests to the agricultural production, forestry and land use sectors that in the medium to long term it is in their interest to keep a significant proportion of their land based carbon credits to cover their own future greenhouse liabilities.

In rewarding early abatement, the Australian Emissions Trading system should establish a mechanism to reward land based sectors for hanging on to their own carbon credits to meet their future liabilities.

Vulnerability 2 Emissions Permits and trading could erode the benefits of additional voluntary action.

The Climate Group will need to look very closely at how the mandatory permit and trade system will interact with voluntary actions so as not to eliminate the greenhouse benefits of voluntary actions by a company selling on their emission permits.

Before it is said that "*that is what the system is supposed to do*", think about this in the context of voluntary actions and claims by organisations. For example, a business may be seeking to achieve sustainability and promote their image as being clean and green by committing to be "Carbon-neutral" or working towards such a target. Assume that this business has a 50% direct emissions liability for its scope 1 emissions and a 50% indirect liability for its scope 2 and 3 emissions. Currently such a business may seek to minimise and offset all of its scope 1 emissions and purchase accredited GreenPower and carbon offset transport fuels, as well as other carbon offsets to deal with remaining scope 2 and 3 emissions, effectively achieving a carbon neutral greenhouse gas inventory. Under the current arrangements all of these actions are additional. Under an emissions trading system however, this business would be eligible for emissions permits for its Scope 1 emissions. It could make claim of carbon neutrality and sell its emission permits to the market thereby allowing another organisation to commence the pollution once more, nullifying the greenhouse benefit of the voluntary action.

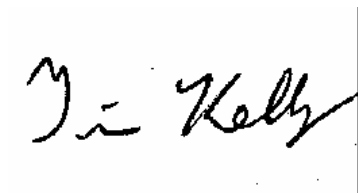
The potential carbon leakage through claiming voluntary greenhouse reductions whilst simultaneously selling emissions permits could be significant and this vulnerability should be dealt with. The issue only arises with a permit and trade system and would not apply to a tax and trade system.

A possible approach to lock in the benefits of voluntary actions would be to allow for the voluntary retirement of permits where businesses can ensure the additionality of their emissions reduction actions. Under voluntary permit retirement approach, the Scheme Regulator would maintain a voluntary permit retirement register in addition to the National register for offsets and early action credit.

To provide market transparency, organisations that make substantial greenhouse reduction or carbon neutral claims should also be required to report the number of emissions permits that they have sold on to other emitters.

Thankyou for providing the opportunity to comment on the Abatement incentives prior to the commencement of the Australian Emissions Trading Scheme.

Kind regards

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