Summary of the Australian Government's climate change plan

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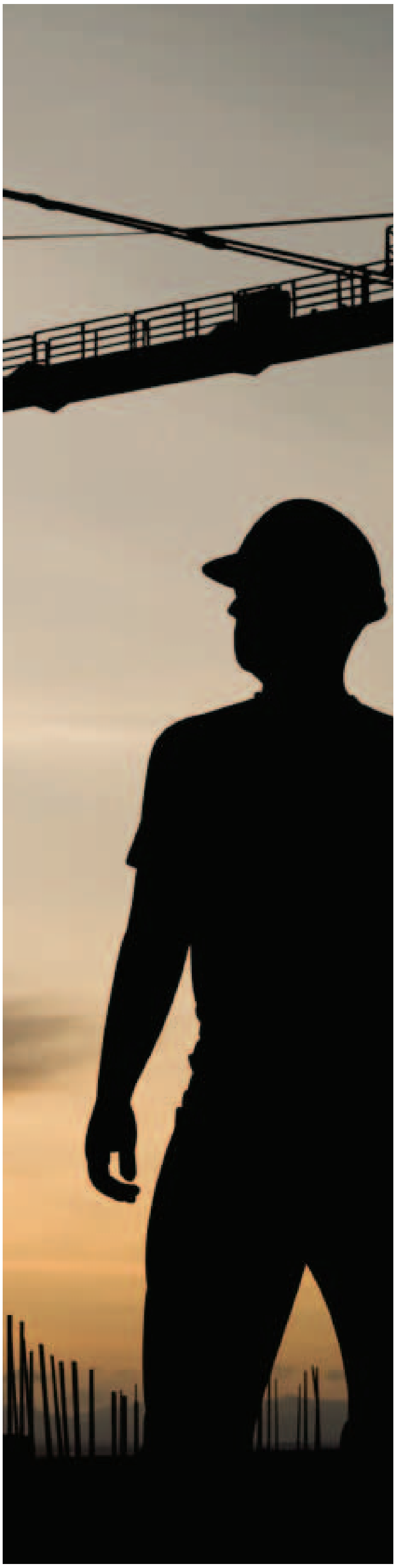

Carbon pricing – the basics

The Australian Government's climate change plan, 'Securing a clean energy future – The Australian Government's climate change plan' can be found at cleanenergyfuture.gov.au

The intention of a carbon price is to influence consumer behaviour away from purchasing high emissions-intensive products to lower emission-intensive alternatives, if such alternatives exist. The higher the emissions intensity of a product, the higher the carbon price on that product will be, assuming that the price increase is passed on to end consumers. Business may respond to this price signal by reducing the emission-intensity of its products to remain competitive or gain a market advantage. The theoretical outcome is Australia's greenhouse gas emissions will be reduced.

Economic modelling predicts that the inflationary impact of the Australian Government's carbon price will be 0.7 per cent. This means the average increase in expenditure across all households is expected to be about $9.90 a week in 2012-13, including $3.30 on electricity and $1.50 on gas. The impact, however, will vary across households and business. How the introduction of a carbon price will affect consumer confidence, which is already fickle, is difficult to predict.

Key elements

Who will be directly liable under a carbon price?

Over half of Australia's emissions will be directly covered by this scheme. Greenhouse gas emissions from the following sources will be covered by a carbon price:

- stationary energy
- non-legacy waste
- industrial process
- fugitive emissions (except decommissioned coal mines)
- heavy on-road vehicles from 1 July 2014.

Within these sources, only facilities with direct (scope 1) greenhouse gas emissions of 25,000 tonnes a year or more will be liable under the scheme. This works out to be about 500 entities being directly liable.

How will a carbon price work?

For those entities that have a direct liability under the scheme, they will have to surrender to the scheme regulator the number of permits (one permit equals one tonne) that is equivalent to their emissions for the year from 1 July to 30 June. For example, if an entity emits 100,000 tonnes from 1 July to 30 June, they will have to surrender 100,000 permits. Permits will generally either be purchased from the Australian Government, purchased from other entities or be received free-of charge-from the government (for certain industries receiving assistance such as steel).

What will the carbon price be under a carbon tax?

A fixed price scheme (carbon tax) will operate from 1 July 2012 to 30 June 2015. The initial price will be $23 per permit (one permit equals one tonne) from 1 July 2012 and increase by 2.5 per cent in real terms for in subsequent years.

What will the carbon price be under an emissions trading scheme?

On 1 July 2015, the carbon price will transition to an emissions trading scheme (ETS). The price for permits under an ETS will vary depending on the number of permits in the market (mainly supplied by the government) and the demand for those permits. However, the market price will not be fully flexible for the first three years of the ETS as there will be a price ceiling and a price floor.

What assistance will be provided to households?

More than half of the revenue raised will be used to help households. The assistance will be delivered in the form of tax cuts and increased welfare payments. The government claims that nine out of 10 Australian households will receive some form of assistance, and of that figure, the government claims that many low income households will receive greater assistance than the impact of a carbon price.

What assistance will be provided to industry?

The Australian Government intends to allocate around 40 per cent of the carbon price revenue as industry assistance to businesses that are highly exposed to international competition and will therefore be adversely affected by a carbon price, such as aluminium production, steel manufacturing, pulp and paper manufacturing, glass making, cement production and petroleum refining. Most assistance will be delivered in the form of free permits, however some assistance (including to the steel and coal industries) will also be delivered by way of grants to help such industries become less emissions intensive.

What is being done to ensure the continuity of electricity supply?

The government will consider providing cash and free permits to help generators that face sizeable asset value losses and may offer loans to generators that can not refinance from the market on reasonable terms. The government will also seek to pay the owners of some very high emissions-intensive coal-fired power stations to close by 2020.

What investment is the Australian Government making in clean energy?

The government will create a financing corporation with $10 billion to invest (through loans or taking equity stakes) in the commercialisation and deployment of renewable energy, energy efficiency and low-pollution technologies, but not Carbon Capture and Storage.

What is the Australian Government doing to reduce myriad existing carbon reduction policies?

The government will create a large independent agency to administer some of the existing schemes that support research and development (R&D), demonstration and commercialisation of renewable energy technologies. There is, however, no clear plan to wind back many of the 230 existing schemes which provide little value for money for taxpayers (in terms of reduction in emissions) for the money spent.

What was announced on research and development?

There is little support in the government's package for general research and development of low emission/clean technology. An effective premium tax credit for research and development into low emissions/clean technology leaves it up to business (and not government) to choose the technology or suite of technologies that will best reduce emissions. This is a major flaw which we hope the government will correct over time (by possibly redirecting the funding of some of the 230 carbon reduction schemes).

Detailed summary of the carbon pricing mechanisms

Who will be directly liable under a carbon price?

More than half of Australia's emissions will be directly covered by this scheme. Greenhouse gas emissions from the following sources will be covered by a carbon price:

- stationary energy
- non-legacy waste
- industrial process
- fugitive emissions (except decommissioned coal mines)
- heavy on-road vehicles from 1 July 2014.

Farming and land-based activities will not be covered.

Within these sources, only facilities with direct (scope 1) greenhouse gas emissions of 25,000 tonnes a year or more will be liable under the scheme. This works out to be around 500 entities being directly liable.

Carbon tax

A fixed price scheme (carbon tax) will operate from 1 July 2012 to 30 June 2015. The initial price will be $23 per permit (one permit equals one tonne) from 1 July 2012. On 1 July 2013, the price will rise 2.5 per cent in real terms to $24.15 per tonne and from 1 July 2014, the price will rise a further 2.5 per cent in real terms to $25.40 per tonne ('real terms' means the CPI figure, which is estimated to be 2.5 per cent).

Other important details of the design of the carbon tax to consider are that:

- the compliance year will be from 1 July to 30 June
- any permits purchased at the fixed price will be automatically surrendered to the scheme regulator in the year of purchase and cannot be traded or banked for future use
- freely allocated permits may be traded in the year they are issued, however they must be surrendered in the year they were issued (in other words, they cannot be banked). Holders of such freely allocated permits will be able to sell them back to the government. The price will generally be equal to the fixed price of permits for that year.
- liable entities with more than 35,000 tonnes of emissions will generally be required to meet their emission obligations in two parts:
  - a progressive surrender of 75 per cent of their emission obligations to the regulator by 15 June in the relevant compliance year (in effect, paying the carbon tax as you go)
  - the surrender of the remaining obligations by 1 February following the end of the compliance year
- for liable entities with less than 35,000 tonnes of emissions, they will only have to surrender permits to the regulator equal to their compliance obligations by 1 February following the end of the compliance year (however, they will be able to surrender permits before that date)
- if a liable entity does not surrender the correct amount of permits, they will have to make good of that shortfall by purchasing the remaining permits at a charge equal to 1.3 times the price they would have otherwise paid for those permits.

Emissions trading scheme

From 1 July 2015, the carbon tax will transition to an emissions trading scheme or a cap-and-trade scheme. From 1 July 2015 to 30 June 2018, the price will not be fully flexible. That is, there will be a price ceiling, which will be set at $20 above the expected international price for permits for that year and will rise 5 per cent in real terms each year, and a price floor, which will be $15 per tonne, rising 4 per cent per annum in real terms. From 1 July 2018, the scheme should transition to a fully flexible emissions trading scheme (that is, with no price floor or ceiling).

Other important details of the design of the ETS are as follows:

- Unlimited banking of permits will be allowed in the ETS.
- Limited borrowing of permits from future years will be permitted. A liable entity will be able to borrow up to 5 per cent of permits from future years and use those permits to meet their current year liability.
- Unless freely allocated, permits will be allocated by auction. There will be advanced auctions of future permits before 1 July 2015.
- No permits from the carbon tax can be carried over to the ETS.

- If a liable entity does not surrender the correct amount of permits, it will have to make good of that shortfall by purchasing the outstanding permits from the government at double the average of permits for that year.
- Permits will not be able to be exported before 2018, except as part of a bilateral link to another ETS.
- The government will set annual caps on emissions on the ETS. In the 2014 Australian Federal Budget, the Australian Government will set out the caps for the first five years of the ETS with the caps extended each year after the scheme commences. Some businesses will want to know these scheme caps well before May 2014 and they will want an indication of caps well beyond the initial five years as they will be making investment decisions on assets with effective lives of 10, 20 or even 40 years.

How will the scheme be regulated?

The government proposes to establish the **Clean Energy Regulator** to administer the carbon pricing mechanism. The Regulator's responsibilities will include:

- assessing emissions data to determine each liable entity's liability
- monitoring and enforcing compliance with the carbon pricing mechanism
- allocating permits, including free permits
- accrediting auditors under the Carbon Farming Initiative and the National Greenhouse and Energy Reporting System.

The government also intends to establish the **Climate Change Authority (CCA)** as an independent body to provide expert advice to government on key aspects of the carbon pricing mechanism and the government's climate change mitigation initiatives. The CCA:

- provide recommendations on future emission caps
- make recommendations on the indicative national trajectories
- provide advice on progress being made (or not made) to reduce emissions to meet targets
- review and make recommendations on household and industry assistance
- provide advice on the price floor and ceiling after 2018.

Who will be liable entities?

The liable entity will generally be the entity with operational control over a facility (as determined under the *National Greenhouse and Energy Reporting Act 2007*) that is responsible for direct (scope 1) emissions of the greenhouse gases covered by the scheme that is at least equivalent to 25,000 tonnes of carbon dioxide and that the facility is in a covered sector (in certain circumstances, a landfill facility need only emit 10,000 tonnes for the facility to be liable). If the facility is jointly owned through an unincorporated joint venture where no entity has operational control over the facility, the liability will be allocated between the joint venture partners based on their proportionate interest in the facility.

The government estimates that about 500 entities will be directly liable under the carbon price.

What greenhouse gases are included in the scheme?

The carbon price will only cover four of the six greenhouse gas emissions covered under Kyoto (the CPRS covered all 6). The gases covered are:

- carbon dioxide
- methane
- nitrous oxide
- perfluorocarbon from aluminium smelting.

Hydrofluorocarbons and sulphur hexafluoride will face an equivalent carbon price through levies under existing synthetic greenhouse gas legislation. The levy will be adjusted annually to reflect the prevailing carbon price.

How will fuels be treated under this scheme?

Household and light commercial vehicles (under 4.5 tonnes) will not face a carbon price on their fuel. Agriculture, forestry and fishing industries will not face a carbon price on their off-road vehicles.

Other business transport emissions from liquid fuels and non-transport emissions from businesses using liquid fuels will be subject to an equivalent carbon price, generally applied by reducing business fuel tax credits by an amount equivalent to that of placing the carbon price on such emissions (estimated to be around six cents a litre). The excise on aviation fuel will be increased by an amount equivalent to what the carbon price would have otherwise been. These measures will commence 1 July 2012.

The Productivity Commission will review the current fuel excise arrangements, including examining the merits of a regime based explicitly on the emission intensity and energy content of fuels.

How will emissions from landfill sites be subject to the scheme?

There will be a lower threshold of 10,000 tonnes for landfill facilities within a certain distance of a covered landfill facility (those with 25,000 tonnes of emissions or more). This is to reduce the risk of waste being transported to landfills in close proximity to avoid breaching the 25,000 tonne threshold. Landfill facilities will not be liable for waste deposited prior to 1 July 2012.

How will emissions from natural gas be subject to the scheme?

Retailers of natural gas will be liable for carbon emissions from the use of the fuels they supply to customers. Large users of natural gas will generally be able to assume liability for their own emissions from the gas they use.

Apart from purchasing permits from the government or another liable entity, how else can a liable entity meet its carbon liabilities?

A liable entity will be able to purchase Kyoto-compliant credits created under the Carbon Farming Initiative to meet part of their obligation. Until 1 July 2015, liable parties will be able to meet no more than 5 per cent of their obligations using Carbon Farming Initiative credits.

When Australia's emissions trading scheme begins on 1 July 2015, it will be linked to a suitable emission trading scheme around the world so that liable entities will be able to buy permits from emission trading schemes in other countries or other credible international markets and use those permits to satisfy their Australian obligations. Until 2020, Australian businesses will have to meet at least half of their annual obligations each year by buying Australian permits.

Detailed summary of the assistance to households and industry

What assistance is the Australian Government providing to households?

The government is providing assistance to households as follows:

- Pensioners and self-funded retirees (who hold a Commonwealth Seniors Health Card) will get up to $338 extra per year for singles and $510 for couples. This will include a Clean Energy Advance of $250 for singles and $190 for each member of a couple. The Clean Energy Advance will be paid as a lump sum in May-June 2012.
- Recipients of the Family Tax Benefit Part A will get up to an extra $110 per child.
- Recipients of Family Tax Benefit B will get up to $69 plus up to $300 in additional support.
- Allowance recipients will get up to $218 per year for singles and $380 for couples.
- All taxpayers earning less than $80,000 will get a tax cut of up to $300.
- Low income households that can show they might not receive enough assistance through the tax cuts or government assistance will be able for an annual, tax-exempt Low Income Supplement of $300.

The adequacy of such assistance will be reviewed annually in the Australian Budget.

Most of the welfare assistance will begin being delivered from beginning May-June 2012

The government propose to increase the tax-free threshold from $6000 to $18,200 from 2012-13 and to $19,400 from 2015-16. To limit the benefit of this increase to taxpayers earning less than $80,000, the government also propose to increase some of the marginal rates. This increase in the tax-free threshold is in part being funded by a reduction in the Low Income Tax Offset (LITO). This policy is moving towards the Henry tax review recommendation of a $25,000 tax-free threshold with no LITO.

Current		2012-13		2015-16	
Threshold ($)	**Marginal rate (%)**	**Threshold ($)**	**Marginal rate (%)**	**Threshold ($)**	**Marginal rate (%)**
6,001	15	18,201	19	19,401	19
37,001	30	37,001	32.5	37,001	33
80,001	37	80,001	37	80,001	37
180,001	45	180,001	45	180,001	45
Tax-free threshold ($)		**Tax-free threshold ($)**		**Tax-free threshold ($)**	
16,000		20,542		20,979	
LITO		**LITO**		**LITO**	
$1,500	4% withdrawal rate from $30,000	$445	1.5% withdrawal rate	$300	1% withdrawal rate from $37,000

What support will the government provide for communities and regions?

The government will set aside $200 million for regions in the event that they are adversely affected by the introduction of the carbon price. The funding will be provided on a case-by-case basis and may include support for displaced workers and their families, support for affected small business, community development programs and economic diversification programs.

What assistance is the government providing affected industries?

The government proposes to provide a range of assistance measures to industries that are expected to be heavily affected by a carbon price. The majority of assistance will be provided as free permits, thus reducing the cost to such industries of meeting their compliance obligations under the scheme. The government expects around 40 to 50 activities to be eligible for assistance.

The main industry assistance measure is the **Jobs and Competiveness Plan**. The main features of the plan are:

- the most emissions-intensive trade exposed industries (those with at least 2000 tonnes per million dollars of revenue or at least 6000 tonnes per million dollars value added) will receive 94.5 per cent of their permits free of charge
- those industries that are little less exposed (1000 tonnes to 1999 tonnes per million dollars of revenue or 3000 to 5999 tonnes per million dollars value added) will receive 66 per cent emissions free-of-charge
- liquefied natural gas (LNG) projects will be eligible for an effective rate of 50 per cent free permits
- new entrants into an emissions-intensive trade-exposed industry will receive the same assistance as existing entities
- the allocation of free permits will be based on historical emissions data of eligible entities
- the assistance rates will be reduced by 1.3 per cent a year
- apart from the annual reduction, there will be no changes to this assistance for the first five years and any negative change for industry must be provided with at least three years notice
- the Productivity Commission will review the effectiveness of industry assistance
- businesses may also make a request to the government to have the impact of the carbon price on their sector assessed, and the government may request the Productivity Commission conduct such a review.

Industry assistance will also be delivered through the **Clean Technology Innovation Program**. This Program will provide more than $800 million (spread over seven years from 2011-12) through grants (minimum grant of $25,000) to manufacturers with facilities that use more than 300 megawatts of electricity, or five terrajoules of natural gas or are liable entities under the carbon price to support investments in energy-efficient equipment and low-emission technologies, processes and products. Funding will be provided on the basis that the government will provide one dollar for every three dollars contributed by eligible business on eligible investments.

All businesses in the food processing, metal forging and foundry industries will be eligible for grants of more than $25,000 to encourage investment in energy-efficient equipment and low-emission technologies, processes and products. Funding will be provided on the basis that the government will provide one dollar for every three dollars contributed by eligible business on eligible investments. The government have set aside $200 million of funding (spread over seven years from 2011-12) to fund this program.

The Australian Government will also provide $200 million over five years (from 2012-13) for grants ($50,000 to $5 million) to support business investment in research and development in renewable energy, low-pollution technology and energy efficiency. The funding will be provided to eligible activities on the basis that the government will provide one dollar for every dollar eligible businesses invest. This figure is significantly less than the $2 billion to $3 billion Professor Garnaut recommended was needed to be invested annually to support research, development, deployment and early commercialisation of new low emissions technologies.

The government will create a **Clean Energy Skills program** worth $32 million to help educational institutions and industry develop the materials and experience needed to promote clean energy skills. As accountants will be fundamental in providing necessary advice to understand the impact a carbon price may have on a business, hopefully some of this money goes to the profession.

What assistance will be provided to the steel industry?

The **Steel Transformation Plan** will provide assistance worth up to $300 million over five years to support the industry to improve environmental outcomes. This assistance is in addition to the assistance the industry would receive under the Jobs and Competitiveness Program (free permits).

What assistance will be provided to the coal industry?

The **Coal Sector Jobs Package** will provide $1.3 billion over six years to the most emissions-intensive coal mines (gassy mines). It will not assist new mines or extensions of existing mines. In addition, the government will provide $70 million over six years to help the coal industry implement carbon abatement technologies.

Small business and the price on carbon

For most small businesses, a carbon price will only result in a small increase in their overheads (as electricity is generally only a small percentage of their overheads). Where possible, businesses should pass on such price increases to their customers, just as they would with any other price increases. The carbon price may also influence investment decisions, for example, making a gas oven more competitive than an electric oven for a bakery.

What support is provided to small business in this package?

Small business will receive support in the form of the following:

- A $40 million program spread over four years will be implemented to deliver information to business and community organisations on the implications of a carbon price and steps to manage the impacts.
- The instant asset write-off threshold will increase from $5000 to $6500 from 1 July 2012 for small businesses with an aggregate turnover of less than $2 million a year. The Henry tax review recommended the threshold be $10,000 so this is a step in the right direction.
- As most small businesses are unincorporated (and hence pay tax under the personal income tax system), many will benefit from the cuts to income tax.

The electricity generation sector

Some interesting facts about the Australian electricity generation sector

- Coal-fired generation accounts for about 75 per cent of Australia's electricity, with gas at 16 per cent.
- Coal produces about double the emissions of gas-fired electricity generation.
- Australia has the highest polluting electricity sector of any OECD countries (as calculated by the average tonnes of carbon dioxide for every megawatt hour of electricity generated).
- Of 80 developing countries only India, Cambodia and Cuba had more polluting electricity sectors.

If Australia is to meet its emission reduction target (5 per cent by 2020 and 80 per cent (was 60 per cent) by 2050), it needs to transform its energy sector from its current high-pollution mix towards a greater reliance on lower (gas-fired generation) and clean energy sources.

Treasury modelling apparently shows that a carbon price together with the government's other clean energy support measures will reshape the future development of Australia's electricity sector. Whether the modelling shows that this policy mix is the most cost effective way to achieve this outcome we are uncertain.

Given the lack of money for general research and development, let us hope that the assistance being planned is sufficiently broad that it allows business to make the choice of which low-emissions technologies to develop, and that the process for accessing grants does not get bogged down in bureaucracy driven by risk aversion, that is, fear of a technology failing – for failure is always part of researching and developing new technologies.

What assistance will be made available to the energy sector?

The Australian Government proposes to establish an **Energy Security Fund** to ensure that the 'lights don't go out'. Under this fund, there will be scope for the government to pay for the orderly closure of very high-emissions intensive coal-fired generation by 2020 (of course this capacity will need to be replaced). A comprehensive structural adjustment support package will be made available to the workforce of generators which contract with the government to close.

The government will also help generators that face sizeable asset value losses through a limited free allocation of permits and cash until 2016-17. It is estimated to cost $5.5 billion and amount to 23 per cent of the coal-fired generation sectors expected carbon liability over this time.

The government, on the advice of a new agency (the Energy Security Council), may offer loans to emissions-intensive coal-fired electricity generators where the generator needs to refinance but is unable to obtain such finance from the market on reasonable terms.

The government will establish an **Energy Security Council** to advise it on emerging risks to energy security and possible support measures to avert risks to supply.

Supporting low emissions and clean technology

How will the Australian Government fund the development of low emissions and clean energy technologies?

The government will establish a $10 billion **Clean Energy Finance Corporation** to invest in the commercialisation and deployment of renewable energy, energy efficiency and low-pollution technologies but not Carbon Capture and Storage (which is covered in existing programs). Such investments can either be made through debt or equity and must be consistent with the investment mandate prescribed by the government.

It is difficult to judge the merit of this fund without seeing its investment mandate. If it is run purely to seek a commercial rate of return, then this will invariably mean that the fund will invest in proven existing technologies, even though such technologies may not generate significant reductions in emissions and do little to meet Australia's future energy needs. The fund must be encouraged to take the risk of investing a significant proportion of its money into researching, developing, deploying and the early commercialisation of new unproven technologies, as we do not know which technology or suite of technologies will lead to large reductions to emissions in the long-run while still meeting our growing energy needs.

How will myriad existing carbon reduction programs be managed?

The Australian Government will establish an independent statutory body, the **Australian Renewable Energy Agency** (ARENA) to administer $3.2 billion in existing Australian Government support for R&D, demonstration and commercialisation of renewable energy technologies. It is unclear whether this body will have a responsibility for advising the government on which of their carbon reduction programs should be wound up because of the poor return (in terms of emission reductions) for the taxpayer. Let us hope that this agency can stop the great big waste of taxpayer money that is going on in many of these programs (at both state and federal level).

Taxation treatment of permits

What will be the taxation treatment of permits?

The taxation treatment of permits will be as follows:

- The cost of a permit will be deductible with the deduction deferred until the permit is sold or surrendered.
- The proceeds of selling a permit through trading will be assessable income in the year the permit is sold.
- Under the rolling balance method, any difference in the value of permits held at the beginning and the end of an income year will be reflected as a variation in a taxpayer's taxable income with any increase in value included in assessable income and any decrease as an allowable deduction.
- Taxpayers will be able to elect to value permits that they hold at the end of the first income year either at historical cost or at market value, with the default being historical cost.
- Taxpayers will be able to change their valuation method once until 30 June 2015 and taxpayers will be able to change valuation again after a method has been in use for four years following the commencement of the ETS on 1 July 2015.
- The value of a permit will be deemed to be its market value where:
  - it is transferred under a non-arm's length transaction
  - it is issued to the taxpayer as part of an assistance measure
  - the permit has been issued under the Carbon Farming Initiative.
- Expenditure incurred in becoming a holder of a permit will be deductible in the year the taxpayer starts to hold the permit, except where the permit is:
  - issued as part of an assistance arrangement, in which case the deduction is denied
  - the permit is issued under the Carbon Farming Initiative, in which case, existing income tax law will apply.
- The *A New Tax System (Goods and Services) Act 1999* will be amended to make the supply of permits GST-free. The transaction of financial derivates of permits will be subject to normal GST rules.

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