



# **Plastics and Chemicals Industries Association**

## **Inter-Jurisdictional Working Group on Emissions Trading**

### **A National Emissions Trading Scheme**

**Background paper for Stakeholder Consultation -12 September 2005**

**Submission by the Plastics and Chemicals Industries Association**

**November 2005**

#### **Introduction**

PACIA is the peak national body for the Australian and chemicals and plastics (C&P) industry sectors. These sectors had a combined turnover of \$31 billion in 2000-01, and directly employed over 81,000 Australians; they represent over 10 percent of all manufacturing output and employment.

PACIA acknowledges that the potential impact of emissions of carbon dioxide and other greenhouse gases on climate change is very significant. It recognises these emissions are a global issue, and that reductions in emissions alone are unlikely to redress this potential impact, and that a range of approaches - involving abatement, capture and adaptation strategies as well as emission reductions - are required, and require global action through the cooperation and support of the community, industry, governments and international institutions.

## **The Australian Chemicals and Plastics Sectors**

The C&P industries are typically energy intensive and trade expose sectors; these industries are widely represented in all developed, and most developing countries. Australia, as a comparatively small and isolated market is not immune from world influences on supply, demand and prices, but for most sectors there is limited opportunity to exploit world markets because of the scale of Australian production and transport costs.

In the comparatively small, open and competitive market of Australia, the capacity of these industries to access low-cost energy and feedstock sources is critical to their survival. PACIA's vital interest in the work of the Inter-Jurisdictional Working group centres on this reality.

### **Emissions Trading - General**

The C&P industries accept that:

- effective action to address the climate change impacts of greenhouse gas (GHG) in emissions requires long-term, global action
- if 'atmospheric' carbon dioxide (CO<sub>2</sub>) and other GHG levels that most science based opinion consider to be sustainable are to be achieved, a dramatic reduction in the global emissions must be achieved in the longer term
- a realistic period for the achievement of these levels is about 50 years, given existing infrastructure and the anticipated opportunities for technological developments
- market mechanisms should play a vital part of an efficient and fair means to achieve CO<sub>2</sub> constraints, and the achievement of an appropriate balance between abatement in emissions, renewable sources of energy, sequestration and other mechanisms to deliver the desired outcomes
- emissions trading should not act as a de facto tax (an annual auction of emission permits would be such a case), and should be primarily focused on efficient mechanisms to meet energy demand and promote the required technological solutions

The C&P sectors recognise that even the simplest model of an emission trading regime is complex, and PACIA has no experience or competence in such arrangements. Against this background, this submission does not attempt to address all of the questions raised in the Background Paper; rather, it focuses on issues where some impact on these sectors could be anticipated if an emission trading scheme were implemented. Nevertheless, PACIA remains concerned that modelling and experience with 'cap and trade' emissions trading schemes have not demonstrated the capacity to deliver the incentives to drive

the required technological and demand change required to to stabilise or reduce atmospheric GHG levels.

## **PACIA Industry Position**

PACIA's key concern relates to energy costs. Specifically, this concern is that GHG emission control and abatement measures which impose costs on domestic producers – costs which do not apply to competing import suppliers - represent an inequitable and damaging impost which threatens the industry's viability.

Energy represents a substantial cost for most products of the C&P sectors, and Australia's reliable energy supply at costs which are low by international standards is vital to these sectors capacity to compete with imports. Much of the import competition in the Australian market comes from Asia - from developing countries which have recognised low labour and other input costs, and protected domestic markets. These countries (which are estimated to account for about one-third of world GHG emissions) have indicated - unequivocally - that they do not propose to implement measures to reduce or abate GHG emissions.

PACIA can add little that has not already been said to support the argument for global and equitable action by all countries if measures to constrain and abate GHG emissions, and to prepare for and adjust to global warming, are going to deliver a meaningful and effective outcome. PACIA accepts that action is necessary, and that there must be implications for energy availability and cost.

However, its concern is fundamental - were Australia to take action on GHGs which increases costs or constrains the availability of energy in Australia, and comparable measures are not applied to competitive industries in Asia, then the domestic industry cannot continue to profitably produce and sell its output. Manufacturing capacity will be lost, and imports will replace local production.

Unless GHG emission reduction or abatement efforts have global application, there is no realistic prospect that measures applied will have a beneficial impact on global warming. Indeed, to the extent that producers in countries not addressing GHG emissions continue to source most of their energy from high emission sources, have less efficient production capacity or require more transport to deliver goods to the market, the net effect may well be to increase global emissions.

As mentioned above, PACIA and its members have actively pursued initiatives to improve energy efficiency, and indicative results are that these initiatives provide, and will continue to provide, significant dividends in reducing GHG admission rates. It recognises that there remains considerable scope for further work in the C&P sectors to improve energy efficiency and abate emissions. In addition to reducing GHG emissions, these initiatives will make a valuable contribution to these sectors' capacity to compete with imports, and continue to contribute to economic activity and employment.

## **Comment on the Background Paper**

Comments below are identified, to the extent possible, against the relevant part of the Background Paper.

### *Issues for Consideration*

The Paper identifies the requirement to maintain 'flexibility to incorporate changes in international policy', but in many respects tends to focus on the Kyoto Protocol and the EU emissions trading scheme, implicitly suggesting that there is an expectation that these models will have wider acceptance. An emission trading scheme developed in Australia now would have little relevance to the target for the 2008 to 2012 period set under the Kyoto Protocol; apart from the fact that a scheme developed now can have little impact on emissions in that period, Australia would not seem to require further emission reductions to achieve its targets. The United Nations Framework Convention on Climate Change has not contemplated targets beyond 2012. At the same time, there have been many other initiatives aimed at addressing GHG emissions and climate change, and an emissions trading regime for Australia must be sufficiently flexible to complement these other initiatives.

In PACIA's view, it would not be possible to effectively implement an emissions trading scheme without all jurisdictions involved. Apart from the complexity and resource efficiency distortions a partial scheme would inevitably involve, it would do little to ensure that other schemes (such as those already implemented by some States) would not proliferate.

PACIA has some concern about an emission trading scheme having the '... potential to generate revenue to support greenhouse gas abatement activities'. An emission trading scheme should allow different sectors of the economy to make decisions as to the means to reduce emissions, use or deploy more carbon efficient energy sources or reduce atmospheric CO<sub>2</sub> through sequestration or other means; it would be inappropriate for such a scheme to involve a taxing element to enable governments to direct abatement, or any other, CO<sub>2</sub> reduction strategy.

### *Proposition 2 - the scheme be national and sector based*

PACIA is concerned that a sector based approach (which, inevitably, focuses on the stationary energy sector) will have a greater impact on the sectors of the economy that are relatively larger users of that form of energy than on other forms, and that the cost pressures and structural demands that result will mean that the burden of improving environmental outcomes is not shared equitably.

### *Proposition 3 - (equity between sectors covered by the scheme and those outside it)*

As commented above, PACIA considers that the immediate Kyoto Protocol target is not an appropriate basis to consider an emissions trading scheme, and that any scheme must be sufficiently flexible to accommodate a range of

prospective CO<sub>2</sub> constraint regimes over the next several decades. Notwithstanding the absence of any clear direction in the international context, it is essential that industry has some clear indication of the longer term constraint objectives, and the ability to obtain permits or other rights to emit CO<sub>2</sub>, if investment and economic growth are not to be adversely affected.

*Proposition 4 - the scheme initially cover the stationary energy sector*

As noted under proposition 2 above, PACIA is concerned about the distortion that could occur if only the stationary sector were constrained by a trading regime. For many industrial sectors, there is little scope to alter the demand for energy, the type of energy (electricity, gas, etc) or the volume of demand if production is to be maintained. In these situations, a scheme based only on these sectors will artificially raise prices of emission trading permits, but may not provided the incentives within the economy for the development of technology to reduce CO<sub>2</sub> levels.

*Proposition 6 - allocation methodologies*

In PACIA's view, it is imperative that an emission trading scheme fulfils the requirement to provide stability in policies and procedures in relation to CO<sub>2</sub> emissions, so that investment is considered by industry against realistic expectations, and that the risks of windfall losses are not unacceptable. Such an outcome would seem to require long-term permits, and commitments from government in relation to those permits such that, were there to be windfall losses (or gains) from changes in policy or procedures, then emission permit holders will be appropriately compensated.

*Proposition 8 - offsets*

In PACIA's view, an emissions trading scheme should accommodate as broad a range of offsets as possible. The advantage of such an approach is that it provides maximum opportunity for achieving the most efficient means of emissions reductions and/or abatement.

While acknowledging that offsets can be a complex exercise, and that additionality – in the sense of emission reductions above the business as usual situation - may be a major challenge, PACIA considers that industries not covered by an emissions trading scheme should be included in an offsets arrangement. Long-term improvements in energy efficiency and use should be included, with the benefits of abatement recognised against realistic baselines in light of economic and production growth.

*Proposition 9 - mechanisms to address adverse effects and structural adjustment*

There can be little doubt that a critical and sensitive aspect of any carbon emissions trading regime is the loss of comparative competitiveness of industries within the regime compared to those not covered by it. It is inevitable that there is a cost associated with reducing or abating CO<sub>2</sub> emission's beyond

those that are achievable through energy efficiency improvements, and emissions trading permits should, and ultimately will, reflect the costs of remission or abatement. As noted above, the migration of industry to non constrained production locations will do nothing to reduce atmospheric CO<sub>2</sub> levels, but will adversely affect those economies with emission constraints in place.

The availability of reliable and low-cost energy to the chemicals and plastics industries is vital to their survival. For many sectors, the size of the domestic market and logistic constraints to substantial export activity mean that the local industry must compete with imports with no realistic opportunity to derive scale and other economies available to competing producers, especially those in Asia. These sectors are typically energy intensive, with energy representing as much as one quarter of factory cost for many producers.

PACIA accepts that there are a number of ways in which the adverse effects of an emissions trading regime on import competing and energy intensive industries can be addressed. The most economically efficient and fair of these is to ensure that the cost implications of a trading regime are not passed through to these sectors - exceptions or free allocations of permits may be appropriate mechanisms. Other forms of assistance such as subsidies or border tax adjustments would only approximate the economic impact of a trading regime, and would in themselves involve costly additional regulatory arrangements.

Exemptions from, and/or free allocations, within an emissions permit scheme should remain in place while the comparative disadvantage they involve continues to apply – in effect, until such time as an effective emissions trading regime, or similar market-based constraint mechanism is global in operation.

*Proposition 10 - transition for early abatement action, new entrants*

The nature and extent of mechanisms to ensure no disadvantage to emitters that participants have taken early abatement action, and new entrants to an emissions permit market, will depend on the nature of the carbon emission trading permits arrangements. Clearly, some mechanisms, such the auction of short-term permits, may not require provisions for early movers and new entrants; other arrangements will require that the legitimate interests of early movers and new entrants are specifically addressed.

In PACIA's view, there should be adequate and appropriate recognition of early movers. In this context, many Australian industries have actively pursued policies to reduce or rebate their carbon emissions since the early nineties, against a background of Government encouragement to do so. It would be appropriate that recognition of early movers cover this period.

## **Conclusion**

PACIA does not support a carbon emissions trading regime. As an energy intensive, import competing and trade exposed sector of the Australian economy, there are significant risks that a carbon emissions trading regime will involve costs that are critical to the competitiveness of the Australian industry compared to the large unconstrained suppliers within the region. The longer term interests of the chemicals and plastics sectors in Australia is best served by government policies which ensure that these sectors continue to have access to reliable sources of energy at competitive prices.

At this stage, Australia does not require such a regime in order that it meet the target emission levels for the period 2008 to 2012 of the Kyoto Protocol. While it is acknowledged that there is broad agreement that effective abatement action be taken, and that that involves a significant reduction in atmospheric carbon levels over the next 50 years or so, the appropriate mechanisms for such action are not clear at this stage, and the nature and role of an emissions trading regime that might constructively contribute to such an outcome cannot be determined.

If a carbon emission trading scheme is to be introduced, then the guiding principles should be to ensure that it affords an efficient, cost-effective and fair mechanism to promote commercial decisions which achieve the desired outcome at the least cost to commercial and other energy users.. On this basis, a trading regime should have international application, apply to all sectors producing emissions, and ensure that the trading regime does not inhibit investment and other business decisions. To the extent possible, a carbon trading regime should not inhibit economic growth and development, and must involve low transaction costs - ie minimal regulatory demand and acquittal of permits use.

PACIA is a member of the Australian Industry Greenhouse Network (AIGN), and has been actively involved with other members of the network in considering the Background Paper. The submission of the AIGN addresses broad industry concerns in relation to a trading regime, and offers constructive proposals for an efficient regime. PACIA supports comments contained in the submission.

***Plastics and Chemicals Industry Association  
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