

# RESOURCESLAW INTERNATIONAL

## RECENT DEVELOPMENTS:

### August 2008

#### ***The Australian Carbon Pollution Reduction Scheme (CPRS)***

##### ***Background***

In December 2007, the Government ratified the Kyoto Protocol, committing Australia to capping its GHG emissions.

In July 2008, the Australian Government issued a 500 page Green Paper on the CPRS.

Commencing in 2010, the CPRS will be Australia's principal strategy to meet its Kyoto target (it could also influence the design of other schemes that are now being considered in other countries).

The Government has adopted a domestic long-term target of 60% below 2000 emission levels by 2050 (a medium-term target for 2020 will also be announced later this year).

The *National Greenhouse and Energy Reporting Act 2007* is already in force and requires all major emitters to register, report and publish their emissions data in advance of the start-up of the CPRS.

##### ***Key Elements of the CPRS***

The CPRS will be a 'cap-and-trade' scheme like that of the European Union.

Permits will be auctioned to all emitters that are covered by the scheme (unless firms qualify for free permits – as to which, see over).

The central element of the CPRS will be the annual 'caps' (that is, emissions limits) that the Government will impose. The caps will be set for the first 5 years and will be extended each year by one year to maintain a constant 5 year horizon.

The Government will also set a 'gateway' or range within which future caps will be set for 10 years beyond the preceding caps. The gateway will be reviewed every 5 years.

The CPRS will be a formal, regulated market for the sale and purchase of what the Government calls 'carbon pollution permits'.

The CPRS will apply to all large emitters (those who emit in excess of 25,000 tonnes pa) in nearly all industry sectors. This will directly affect around 1000 firms in Australia and is likely to catch 75% of Australia's total emissions.

The main unaffected sector is agriculture. This will not be included for another 5 years due to the difficulty of measuring emissions from the wide range of different agricultural activities.

##### ***What Will Be the Price of Permits?***

No-one can predict the price as it will depend vitally on the annual caps that are imposed (unless the Government decides to arbitrarily fix the price for a transitional period).

Many commentators have speculated that the permit price will be around A\$20 at the time of scheme commencement. The price will however be determined by levels of supply and demand in the market and could be lower or much higher.

If a price of A\$20 at the time of commencement is assumed, the cost for a low-level emitter that emits 25,000 tonnes pa would be A\$500,000 pa.

##### ***The Pricing Dilemma***

The dilemma facing the Government is that a low permit price is unlikely to induce a significant shift towards a low-carbon domestic economy. On the other hand, a high price would inflict great and possibly irreparable damage on many firms and on the entire economy - without appreciably reducing the level of global emissions (which are likely to continue rising until a comprehensive global scheme has been achieved and put into full effect).

There is a serious risk that the CPRS could fail to make a significant contribution to the reduction of global emissions, if emissions rise at a greater rate in other parts of the world. Fixing the domestic caps in this period of great uncertainty poses a dilemma for the Government.

In this context, the medium-term outlook for the CPRS may hinge on whether there will be a breakthrough in forging a comprehensive global agreement at the Copenhagen Conference at the end of 2009.

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### ***Impact of the CPRS on Firms***

Each firm in the Australian economy will be impacted not only by the direct costs that are incurred in relation to its own emissions but also by the indirect costs from the increased prices of its production inputs (such as higher-priced electricity). This impact will be lessened to the extent that firms are able to pass on their increased costs to consumers.

### ***Transitional Assistance to Firms***

There will be an electricity sector adjustment scheme to soften the impact of the scheme on coal-fired electricity generators.

Emissions-intensive, trade-exposed industries, such as LNG and metal producers, will be unable to pass on their increased costs to customers because of competition from exporters in other countries that do not impose an emissions penalty.

The inclusion of trade-exposed industries in the scheme is likely to diminish the international competitiveness of many existing investments and will scare off new investments in these industry sectors unless special provision is made for their continuance.

For many of these industries, the Government may give them transitional assistance by allocating around 30% of the total scheme permits for free. Eligibility for free permits, and whether the level of transitional assistance is adequate, remain hotly debated issues.

### ***How to Meet the Emissions Targets***

As presently proposed by the Green Paper, affected firms will be able to meet their emissions targets in 5 main ways:

- (i) by purchasing permits, either at the auctions or in the secondary market;
- (ii) by using less emissions-intensive energy sources;
- (iii) by switching to more efficient production technology;
- (iv) by cutting back production; or
- (v) by investing in abatement schemes.

Examples of abatement schemes are forestry projects in Australia and various types of Clean Development Mechanism (CDM) projects in developing countries.

### ***Submissions to Government***

Submissions to Government on the Green Paper must be made by 10 September 2008.

### ***Further Information***

Our managing director Robert Pritchard can be contacted for further information on this Bulletin at [robert@resourceslaw.net](mailto:robert@resourceslaw.net).