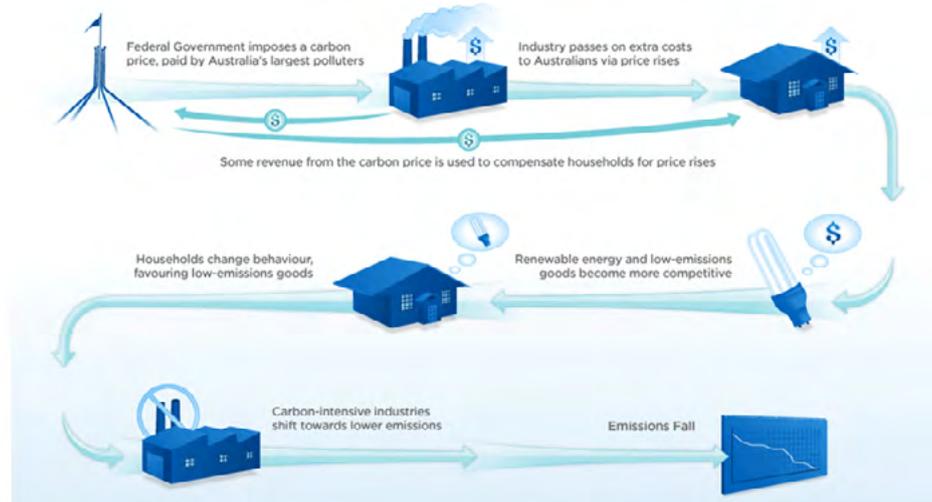


## AUSTRALIA'S 'CARBON TAX'

**Australia**

May 2012

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**Figure one:** Australia's carbon pricing initiative explained.

**Source:** Australian Broadcasting Corporation - <http://www.abc.net.au/news/specials/climate-change/pricing-explained/>



### Policy details

Australia's carbon price package, which was introduced by the government in July 2011, is commonly referred to by the government, opposition, media, and public, as Australia's 'carbon tax'. It is not however, a tax – it is an emissions trading scheme (ETS) with a fixed price.

Within a carbon tax system, a price on carbon is set, and emitters are charged per tonne of carbon they release into the atmosphere, leading people to reduce their emissions to avoid the tax and save money. There is no limit ('cap') to emissions within a tax-based system – people can emit as much as like, but have to pay for these emissions. Therefore, it is the price on carbon that influences emission levels.

In contrast, an ETS mandates a cap on total carbon emissions, and requires emitters to hold a permit for each tonne of carbon that they emit. The cap level determines the number of permits that are available. If emitters don't possess a permit, they must reduce their emissions, or purchase a permit from another emitter, who must then reduce their emissions. Consequently, the cost of emitting is equal to the cost of buy-

#### Quick facts

Zone	National territory
Topic	Carbon tax. Emissions Trading Scheme (ETS)
Starting date	1 July 2012
Implementing Agency	Australian government



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ing or selling a permit. Unlike the tax-based system where it is the price on carbon that leads to emissions reductions, in an ETS it is the cap that determines the level of emissions, and it is the required emissions reductions that determine the cost of emitting carbon. Permits have a value because they allow emitters to avoid making emission reductions.

The system that will be implemented by the Australian Government commencing on the 1 July 2012 is a modified ETS. It involves a cap on emissions with tradable permits (consistent with an ETS), but the price of those permits will be fixed (similar to a tax-based system), at \$23 a tonne, by the government for the first three years. This is most likely a measure which aims to reduce uncertainty during the transition period after the scheme commences. After three years, the system will move to a standard emissions trading scheme, where the price of a permit will not be set by government, but will be determined by the market.

Putting a price on carbon creates a financial incentive to reduce carbon emissions that will flow through Australia's economy. Only the top 500 carbon emitters in Australia are subject to the scheme - 0.02 per cent of Australia's 3 million businesses. Fuel suppliers and distributors and companies emitting synthetic greenhouse gases, including the refrigeration and air-conditioning industries, will be exempt.

Households will not have to pay for emissions permits directly, but will do so indirectly as businesses pass on some or all of the higher costs they face. The price of certain goods that emit carbon as a by-product of their production will increase. However, the majority of Australians will be compensated for this cost. The government has promised that 90 per cent of households will be compensated in some way, with 70 per cent fully compensated through tax cuts, higher family payments and/or increases in pensions and benefits, to counter the increased living costs. Funds generated from the initiative will also be invested into the development of the renewable energy sector, or to achieving energy efficiencies.

The carbon price scheme will drive a cleaner future for Australia as companies seek to reduce their carbon footprint in order to lower costs and remain competitive. New 'green' businesses will also emerge as low emission businesses become more competitive with traditional businesses, who now have to internalize the true and full costs of production by accounting for the external impacts of their processes on the environment.

*Figure one on the first page is a diagrammatic explanation of how Australia's carbon price package is expected to work.*

Modeling by the Australian Treasury demonstrates that Australia's economy will continue to grow strongly with a carbon price. Extensive analysis by economists and independent institutions such as the Productivity Commission has demonstrated that market mechanisms like a carbon price or an emissions trading system are the most efficient and economical ways of reducing carbon emissions.

Australia's carbon price package is a step in the right direction, creating a framework upon which further enhancements can be built. It provides certainty for business and the public, and will be critical in Australia's ability to become a low-carbon economy, and play its part in addressing global climate change.

### Policy challenges

The price on carbon package has been a hotly debated and controversial topic in Australian politics and society in general. One of the greatest challenges has been in effectively communicating how the introduction of a complex economic instrument will impact the average Australian. Like any complex and politicized issue, the public have become even more confused by the misinformation reported by commentators who do not properly understand the issue, or the propaganda from industries which will be affected by a price being put on carbon, who have cited 'job losses', 'higher costs for households', and 'moving business offshore' without sufficient evidence, to influence public opinion.



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Along with providing assistance to households, the plan will provide assistance to Australia's emissions-intensive trade-exposed industries. There is a valid role for government in protecting industries by exempting them from some of their carbon emissions costs, where there is a realistic threat that 'carbon leakage'<sup>1</sup> could occur. However, analysis by the highly respected, independent policy think-tank the Grattan Institute found that proposed the levels of protection that will be provided to the black coal, liquefied natural gas and steel industries is unjustified and costly, and will increase costs borne by the rest of the community to achieve Australia's emissions reduction targets. Fortunately, assistance is only guaranteed for the first 5 years, and the legislation requires the Productivity Commission to investigate the continuing need for this assistance. The Grattan Institute recommends that the Commission should be given the scope to review protection in the wider public interest, by applying a true carbon leakage test.

Overall, the carbon price package is a "good" tax relative to a number of other taxes (such as stamp duty), as the financial burden will be shared widely across Australia's economy, roughly proportionate to consumption, and it will encourage people to avoid emitting carbon, by changing their personal purchasing and consumption choices. With a net increase in the

costs of production, average living standards in Australia will inevitably grow more slowly for a time. However, increased efficiencies and the avoided consequences of climate changes will lead to financial savings, and ultimately the greater well-being of all current and future Australians and citizens worldwide, in the longer term.

### References:

The following documents informed the development of this paper:

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*Productivity Commission (2011). Carbon Emission Policies in Key Economies: Productivity Commission Research Report. Canberra, Australia.*

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<sup>1</sup> Carbon leakage occurs when the introduction of a price on carbon results in production shifting overseas without any net reduction in global emissions