



**Australian Services
Roundtable**

Securing a Sustainable Future in the Global Services Economy

Submission in response to the Carbon Pollution
Reduction Scheme Green Paper

September 2008

This is a Submission from

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Purpose

This Submission to the Department of Climate Change is in response to the Carbon Pollution Reduction Scheme Green Paper July 2008.

Australian Services Roundtable

The Australian Services Roundtable (ASR) is a not for profit company limited by guarantee. We are the voice of Australian services, a peak body for the broad services sector at national level. Our members include both individual organizations and other industry bodies. Our mission is to create a better business environment and ensure international competitiveness for Australia's services industries. ASR's current membership covers;

- Telecommunications
- Financial Services (banking, insurance, securities, funds management & investment services)
- Professional Services (accountancy, legal services, engineering, architecture, design, consultancy)
- Education
- Tourism
- Information Technology, Computer & Manufacturing Services
- Standards & Conformance Assessment Services
- Transport
- Logistics
- Audio-visual services
- Media
- Personal, Entertainment & Cultural
- Other Business Services
- R & D Services
- Health Services
- Environmental Services
- Energy Services
- Mining Technology services

Executive Summary

The Australian Services Roundtable membership supports Government action to reduce greenhouse emissions and accepts that to this end, business can not continue as usual.

Taking a broad sectoral perspective, we recognise that the services sector's relative international competitiveness will be impacted, but we do not seek special "exemptions" from the costs of the adjustments proposed by the Government.

Under the proposed scheme, the services sector at large will bear the costs associated with Government assistance to other, more carbon-intensive, industries to help them with the process of internalizing the price of carbon. This effect on the services sector needs to be better understood in the public discourse.

The Australian services sector is already at the receiving end of net negative effective protection and this current prejudice to the sector as a whole is set to grow as the most carbon-intensive industries receive the significant adjustment assistance currently proposed by the Government.

We are naturally concerned that the subsidy element in the proposed scheme dilutes the opportunity for the services sector to provide positive solutions. It weakens the market signal for development of next generation energy and diverts much needed funding away from national interest infrastructure and away from the commercialization of innovation that can deliver that infrastructure.

Our chief intention, therefore, in putting forward this submission, is to emphasise the need to work towards achieving a more level playing field between industry sectors so that market forces can optimise our economy for a lower carbon world.

Transitional measures which differentiates between industries on the basis of "carbon intensity" will act to the detriment of most of the services industries which tend to be misperceived as "unaffected" by carbon policy. Services have a major role to play in the adjustment to the new economy and must not be ignored in the policy design process.

We note, moreover, that ultimately all Australian industries, increasingly, are price takers, at least to some degree, on the global market. Policies based on increasingly erroneous industry differentiation with respect to "trade exposure" need to be

avoided. Transitional adjustment policies introduced to facilitate commencement of the economic shifts in production and consumption required must be truly temporary and designed not to become de facto permanent. This is in any case essential for reasons of WTO compliance.

Against that background, we ask that the Government, at a minimum, hold a firm line in extending further carve outs beyond those already proposed in the Green Paper. Every additional carve-out will delay the shift in economic activity towards industries and technologies with lower carbon footprints.

Government support, where it is required, would be better focussed on accelerated depreciation and other tax reforms, on support for innovation and investment in infrastructure and associated regulatory reform. And as in all public policy-making, it is critically important, with respect to the design features of the CPRS, to avoid favouring existing industries over new market entrants.

With respect to the speed of the Australian economy's adjustment towards a lower carbon footprint, our view is this should be decided in the context of the Treasury modelling and the research undertaken by Professor Garnaut and should preferably be such as to stimulate and enable a net positive impact on innovation, productivity and economic opportunity. Among other factors to be considered are: the international environment; the capacity of the economy to absorb the "shock" of the carbon trading proposals and the anticipated positive impact of associated complementary policy measures.

We note, however, that the slower the trajectory, the longer Australia will delay achievement of a level playing field – and the longer the services sector will bear the costs which, in the interests of economic efficiency, should more appropriately be shared with other sectors. Also, the slower the trajectory, the greater the disincentive to rapid commercialization of the critically important climate change solutions that services providers can offer.

Submissions from many of our members draw important attention to the fact that the CPRS will not, by itself, deliver the carbon abatement targets required and call for a suite of complementary measures to support the scheme.

It is clear from these submissions that with the right complementary measures in place, very significant energy efficiency gains could already be achieved with known technology.

We also know that radical technological change will ultimately be required to minimise Australia's carbon footprint while maintaining standards of living. Services innovation will be an integral part of that process. We see it as essential, therefore, that the Government focus on establishing the market conditions and regulatory and tax environment that will maximise the development and application of new technologies and generate investment in the associated infrastructure.

It will be clear from our comments that as well as difficulties, we also see major opportunities for the Australian services sector in a world transitioning to a lower carbon economy. Implementation of the CPRS should be designed, as far as possible, as a major opportunity for Australia to develop innovative new industries that facilitate new patterns of production and consumption.

Australia has an opportunity for example to develop best practice financial markets to support carbon trading. As a sophisticated, knowledge-based economy, with many carbon-intensive industries, we are in an excellent position to develop highly saleable expertise in these areas within our services sector.

It is essential, therefore, that the scheme not embed any accidental bias against local development of skills and technologies in Australia. Spending of revenue raised from the emissions trading system should also take account of emerging industry opportunities.

The future prospects for these industries will depend on Australia's international trade policy and profile as well as on environmental policy-making. Policies which appear to be protectionist, judgemental or isolationist will have serious and adverse effects on the Australian services sector's ability to engage in and expand into emerging international markets.

Finally, the Green Paper recognises that a strong monitoring, reporting and assurance regime is needed to ensure that emissions reported under the scheme are accurate and transparent. To that end, the Government needs, in our view, to set out a policy framework for an appropriate level of expenditure on measurement and measurement research, taking account of international, Australian and other relevant standards.

1. Globalisation of Services

“Many businesses will be little affected by the scheme, as they face the same cost increases as their competitors. However, trade-exposed industries may not be able to pass on the costs...”¹

The Australian Services Roundtable (ASR) recognises that the Government is about to take decisions on addressing climate change which will have far reaching effects on the absolute and relative status of all Australian industries.

Too much of the focus has been on the most carbon intensive existing industries which are “trade exposed” and the likely effects of the proposed design features on these industries.

It is crucial that consideration of climate change policy be framed in the context of the larger picture of the Australian economy and of our relationships with our trading partners. Supporting international competitiveness in the broadest sense, not just in carbon intensive industries, is the key to maximizing Australia’s economic future.

Services constitute two-thirds of world gross domestic product (GDP). Services are intrinsically people-intensive industries and constitute the source of most global job growth over the last decade.

In Australia, services account for 78 percent of GDP and 60 percent of domestic investment. Services employ 8.5 of every 10 Australians, with all net job growth over the past two decades taking place within the services sector. Most services firms are small and medium sized and their interests tend to register inadequately on the policy radar.

But Australia’s services firms are globalising fast, in an effort to take advantage of the big new export opportunities. Services exports in 2005, as measured by the ABS, were \$37b and growing at about 4 percent a year:

- Tourism \$11b
- Passenger Transport \$7.5b
- Education \$7b
- Finance & Insurance \$1.5b

At 23% of total exports, services exports are already larger than rural exports and roughly on a par with manufactures exports. But this is known to be a significant under-statement.

¹ Carbon Pollution Reduction Scheme Green Paper July 2008, p.27

The services sector makes a much larger contribution to exports than its direct share, as services are often integrated with other goods. The ABS data suggest that, on average, about one-fifth of the value of Australia's goods exports is composed of services.

The Balance of Payments (BoP) data also does not measure services exports delivered via offshore commercial presence (branches overseas) or franchises. Recent ABS surveys of Australian-owned foreign affiliates show the BoP is probably picking up less than one third of the actual "exports" of services taking place. Recent EFIC data shows Australia's offshore investment flows now exceed inward investment flows, reinforcing the evidence of significant unmeasured services "export" activity.²

Many services industries are meanwhile facing significant challenges in the global market. There are warning signs of potential decline in Australia's competitiveness, including price sensitive slowdown in in-bound tourism and exports of education and IT services, declining share of Australian services exports in global services trade and widespread knowledge-intensive skills shortages. The services unions and employer firms alike rightly worry that Australia is not attracting its potential share of global work onshore.

It is important, against that background, to recognise that all Australian industries, increasingly, have a significant degree of "trade exposure" and will face competitiveness challenges as we move to internalise the price of carbon.

2. Sharing the Burden

"Broad coverage reduces the costs of cutting pollution- the scheme will cover the bulk of Australia's emissions..."³

The proposed CPRS applies to around 1,000 entities with "direct emissions of 25,000 tonnes of carbon dioxide equivalent or more"⁴. For the time being, the scheme excludes agriculture (15.6% of emissions), and land use, land change and forestry

² Importantly, services contributed more than half the companies on the Global100 compiled by IBISWorld/EFIC of Australia's top international companies by foreign revenue. Many different service industries are involved including: financial, property, engineering, transport, communications, media and consumer services. Moreover, the world's top companies in many service industries such as engineering, architecture, property management and analytical services have a strong representation from Australian firms.

³ Carbon Pollution Reduction Scheme Green Paper July 2008, p. 15

⁴ Ibid, p.35

(6.9%)⁵. It then proposes, from among the 1,000 entities, a subset of 'carve-outs' to mitigate the effects on those industries considered most likely to be damaged; (20% of permits, excluding agriculture or 30% when agriculture becomes covered). In addition, 'strongly affected industries', primarily coal fired power generators, receive financial compensation. Further financial compensatory measures are proposed for consumers.

The Government's objective is to achieve broad coverage in order to reduce the cost of the CPRS. But every carve-out allocates a greater share of the cost burden to the rest of the economy. The fact is that the services industries with the lower relative carbon footprints, irrespective of their degree of trade exposure, will bear the bulk of the burden.

We note that this may have implications for Australia's competitiveness in a number of existing services industries, such as tourism, as well as in new and emerging services markets.

Implementation of the scheme should be designed, as far as possible, as a major opportunity for Australia to develop new industries that facilitate new patterns of production and consumption.

We therefore ask that, at a minimum, the Government hold a firm line in refusing any further distortive carve-outs and subsidy elements. Our preference is for positive support programs to address market failures for example via green depreciation and support for innovation.

It is also essential that all carve-outs and industry compensation measures adopted are clearly identified as finite and transitional structural adjustment assistance, to ensure compliance with our WTO obligations.

Implementation

Administration

Implicit in the Green Paper proposal is that the Government will raise revenue, and redistribute it, via the emissions trading system. We are concerned that there may be high administration costs involved in the auction, collection and redistribution process

⁵ We note that exclusion, for the time being, of land clearing and forestry in particular, seems unfortunate as it risks discouraging early implementation of a number of potential soil carbon abatement and replenishment options.

proposed. We would be supportive of design features oriented to minimizing the administrative burden.

Monitoring, Reporting and Measurement

The Green Paper recognises that, given the central role of emissions data to the scheme, a strong monitoring, reporting and assurance regime is needed to ensure that emissions reported under the scheme are accurate and transparent. We also see a need for ongoing statistical review and assessment of the impact of the scheme on carbon abatement outcomes.

To that end, the Government needs, in our view, to set out a policy framework for an appropriate level of expenditure on measurement and measurement research, taking account of international, Australian and other relevant standards.

The National Measurement Institute (NMI) is responsible for coordinating Australia's national measurement system, in line with international legal and technical frameworks. Greater consideration should be given to using NMI's measurement expertise, and avoiding its duplication within the Department of Climate Change.

Appendix D of the Green Paper, *Analysis of the emissions intensity of Australian industries*, illustrates the importance and complexity of emission measurement and reporting. Appendix D reports emissions on the basis proposed for the determination of emissions for the purposes of Emission Intensive Trade Exposed assessment. This is not the same basis as proposed for the CPRS where indirect emissions are not included.

To aid public debate and understanding, the Department of Climate Change should also publish its estimates of the emissions by industry on the same basis as proposed for the CPRS.⁶

Appendix D shows, for example, that Black Coal contributes 5% of Australia's national emission of greenhouse gases, and Aluminium production contributes 6.1%. We note that there are significant problems with the accuracy of the current methods of calculating emissions from coal mines⁷, and that if only direct emissions were

⁶ See also the National Australia Bank submission, which seeks "further clarity regarding the boundaries of (the National Greenhouse Energy Reporting System's) operational control and the assurance framework to ensure the correct information is being reported" and the Commonwealth Bank submission, which gives high priority to the need for rigorous and transparent disclosure and reporting mechanisms.

⁷ The Australian Coal Association in its submission states "Unless these emissions are measured accurately it could lead to serious overcharging or undercharging for individual mines and that in turn could create issues of equity and distort competitiveness between mines, CSIRO research

considered the estimated emissions from aluminium production would be less than 1%.

Governance

ASR recognises the need for the Government to balance policy flexibility in a fast changing environment with the need to provide certainty for industry and investors. We are concerned, however, that the CPRS mechanism could operate as a stand alone artefact under the proposed arrangements (see the discussion of complementary measures and policy linkages below). As previously stated, the policy focus on the carbon intensive sectors of the economy inherent in the scheme excludes much of the economy from immediate active participation.

In considering the structures and institutions involved in CPRS governance, we believe that the Government should include a broadly based industry advisory body as an integral part of the decision making process.

4. Complementary Measures

Many of our members have identified a broad range of energy efficiency measures which if implemented would have the potential to generate long term carbon emissions reduction reasonably quickly and at a relatively low cost.

We therefore call for early action to implement a suite of complementary energy efficiency (as well as carbon absorption) measures. Such measures need to be complementary on two levels.

First, complementary measures should facilitate constructive interaction by all sectors of the economy with the participants in the CPRS, specifically in order to achieve any given emissions "cap" at the lowest possible "price".

Complementary measures should be designed, that is, to encourage active development of effective alternatives for industry and consumers to simply paying higher prices for energy – indeed a number of them could help buffer against rising energy prices and perceived energy security risks. Many such outcomes are already achievable with known technology, for example in the built environment. The Australian Sustainable Built Environment

shows that existing methods of measuring fugitive emissions are subject to large variations and substantial errors."

Council (ASBEC) has released a report⁸ which estimates that implementing energy efficiency in the building sector could deliver 60 mega tonnes of carbon abatement per annum by 2030 and reduce the price of carbon permits by up to 14 percent. We call specifically, therefore, for green depreciation measures to facilitate new fit out of all buildings including all tourist accommodation.

Carefully targeted complementary measures could also help to stimulate the emergence of new technological and non-technological solutions which can enable new patterns of production and consumption and have speedy and significant beneficial impact throughout the supply chain.

The resulting solutions would naturally also have significant export potential – not only in the context of trading partners' desire to reduce carbon emissions, but more broadly as smarter, cheaper ways of doing business. There is scope for complementary measures to assist the achievement of other related national priorities such as promotion of innovation, skills development and trade.

In addition, the Government needs to focus on other more broadly complementary measures to ensure that the market conditions exist to stimulate investment in the new lower carbon economy. This includes focussing on regulatory reforms to address the market and systems failures currently detracting from innovation.

Specific Proposals for Consideration

Accelerated or Green depreciation for commercial buildings - involves the provision of accelerated depreciation allowances for capital expenditure on refurbishments that 'green' existing commercial buildings, ie expenditure on energy efficient fittings, fixtures and capital works that raise the overall energy performance of the building to a specific standard. Green depreciation would play a key role in overcoming the timing gap problems, allowing investors to defer tax payments in exchange for bringing forward energy efficiency and greenhouse gas reductions.⁹ Green depreciation has a major role to play across other industries also.

⁸ Australian Institute of Architects submission to the Department of Climate Change. See also the Australian Sustainable Built Environment Council (ASBEC) submission.

⁹ Australian Institute of Architects submission to the Department of Climate Change, p.5. See also the Australian Sustainable Built Environment Council (ASBEG) submission, pp29-30.

Measurement of energy efficiency potential, targets and outcomes – current policies and programs directed at energy efficiency are fragmented and data to identify areas with the highest potential and best results are lacking. Good measurement would assist Government in prioritising policies and programs, and improvements achieved could be factored into the setting of CPRS caps.¹⁰

Targeted support for innovation – identify innovation streams with commercial potential for significant efficiency gains and link with Cutler Review responses.¹¹ Options include tax concessions and credits, research grants and development of best practice models and efficiency targets in the public sector. Incentives should be provided for both existing entities and new market entrants to design and implement business innovations which reduce emissions.

Regulatory review and reform– identify and remove regulatory impediments to increasing energy efficiency, and to private investment in innovation and infrastructure.

The Henry Review of Taxation will need to give urgent consideration to the need to align tax incentives with the objective of reducing carbon emissions¹², the application of the GST, the role of State and Territory taxes, application of accounting regimes and the treatment of both regulated and unregulated legal obligations¹³.

Other regulatory concerns include the application of accounting standards, implementation of the emissions reporting regime, and treatment of price regulated products and services.¹⁴ All of these areas have the potential to unnecessarily increase the regulatory burden on business and discourage investment.

Appendix; Other Policy Design Options

In proposing an emissions trading system, rather than for example a carbon tax, the Government is opting to intervene on the supply side (by setting the “quantity” of carbon permits) rather than on the demand side (by setting the carbon “price”).

We note, however, that the specific scheme proposed in the Green Paper attempts to set not only the quantitative “cap” but

¹⁰ Engineers Australia submission to the Department of Climate Change, p.10.

¹¹ Environment Business Australia submission to the Department of Climate Change, p.16.

¹² Some options are outlined in the Telstra Corporation submission, recommendations 7,8 and 9.

¹³ Ibid, recommendations 10 and 11.

¹⁴ Ibid, recommendations 12-16.

also, via the initial auction amongst a limited set of participants, the “price”.

The scheme proposed therefore has a price-based, or tax-like element. We are concerned that over-intervention along these lines may over time open the scheme to the risk of unpredictable consequences.

General principles underpinning one approach which we consider may be worthy of further consideration as greenhouse policy evolves, is an economy-wide base-line cap and trade model, in which the total quantum of permitted emissions is capped, all firms over a certain size are allocated an emissions quota of permits and all firms then trade permits to determine the price of carbon.

Such a model would have the advantage of allowing complementary measures to improve carbon absorption or energy efficiency (such as a national system of “white certificates”) to be built readily into the system in a market-oriented manner. Energy efficiency and carbon absorption “certificates” could be traded, for example, in sub markets to help reduce the demand pressures for carbon permits.

Such a model would have the further advantage that it would not draw Australia into WTO dispute territory.

In drawing attention to this alternative option of an economy-wide base-line cap and trade model, our objective is not to slow down, nor accelerate, the speed of adjustment. The speed of adjustment is a function, in an emissions trading system, of the “cap” and we leave that decision-making to be made on the basis of rational economic modelling and Government policy in the light of international developments. Our interest in the option of a national base-line cap and trade model is solely based on our orientation to a more fully market-based solution.

Some commentators are, meanwhile, calling for reconsideration of a carbon tax as an alternative policy option. In reflecting on this commentary, we observe that interest is also reemerging internationally, both in the potential efficiency gains to be gained via implementation of a global carbon tax as well as the possibly greater prospects of achieving global agreement on a carbon “price”, as distinct from a set of national “quantity” targets.

From a global perspective, we retain an open mind on this matter.

As with an emissions trading system, however, (only more so) we would be very wary of the trade implications of, and WTO constraints on, the various potential design features of a national carbon tax and in particular of any adjustments or “carve-outs” at the border.