

AUSTRALIAN ENVIRONMENT BUSINESS NETWORK

Review of the Protection of the Environment Operations Amendment (Tradeable Emissions Schemes) Bill 2000

November 2000



Sydney & Melbourne

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EXECUTIVE SUMMARY

The Australian Environment Business Network is a new organization representing the interests of industry and business operating in NSW and Victoria.

Introduction of the Protection of the Environment Operations Amendment (Tradeable Emissions Schemes) Bill 2000 (POEO A (TES)) was introduced into Parliament with no prior consultation or reference to industry or business, let our members. Any piece of draft law that is pushed through in such a manner always raises the concerns of industry and business. Generally most are minor in nature and do not generate comment. However the POEO A (TES) Bill on review raises many issues and has led to the preparation of this submission in response.

AEBN considers the use of tradeable emission schemes have merit if used properly and cost-effective. Consequently, the principles of the POEO A (TES) Bill are of less concern than its proposed implementation. Of concern is the absence of appropriate checks and balances on the Environment Protection Authority (EPA) implementing tradeable emissions schemes. Through omission or design the Bill would give new powers directly to EPA staff, powers that are currently only available to the Minister.

Under most circumstances the canceling of a participant from an emissions trading scheme will result in the cessation of activities at that site. The operation will be closed down and jobs will be lost. Powers which can shut down industrial sites are quite rightly the Minister's prerogative. However, there are many different means under the POEO A (TES) which this outcome can occur through EPA officer discretion. As a consequence of the lack of checks and balances AEBN has recommended a number of changes to the Bill including:

- All regulations made under sections inserted by the POEO A (TES) Bill to be subjected to the normal regulatory review process requiring repeal and remaking every five years
- Appeal rights on conditions inserted in POEO licences by Tradeable Emission Scheme regulations to be restored.
- Any action that has an outcome which will result in a site closure to be within the Minister's Ministerial powers and decision as consistent with the POEO Act
- Special constraints to be placed on the EPA in its operation and trading within the markets it controls

Use of tradeable emissions schemes have been used overseas and in NSW they serve a useful purpose, being flexible for industry and requiring low levels of Government resources to operate while achieving worthwhile environmental outcomes. AEBN is concerned that some schemes will be implemented which do not offer these benefits, but merely serve the interests of the regulator without achieving notable environmental outcomes in a cost effective and efficient manner.

RECOMMENDATIONS

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- R1 AEBN recommends that any tradeable emission scheme regulation be subject to the full Regulatory Review process including a comprehensive Regulatory Impact Statement, public participation and five year repeal and review process. 2
- R2 AEBN strongly recommends that subsections (2) and (3) be omitted and all appeal rights on EPA licences for the purposes of the tradeable emissions scheme regulations be included. 3
- R3 AEBN recommends that any late payment or error done in good faith should not be subjected to penalties and be consistent with section 295K which exempts the EPA from liability. 3
- R4 AEBN recommends that any penalties should not incur interest rates exceeding that of the Australian Tax Office. 3
- R5 AEBN recommends section 295E(3)(a) and (b) be amended to :
- (a) the quantity of pollutant emitted by the participant in contravention of the scheme, as estimated by the EPA and agreed to by the Load Based Licensing Technical Review Panel.
 - (b) the amount of monetary, financial or other economic benefits obtained by the participant as a result of contravening the scheme, as estimated by the EPA and agreed to by the Load Based Licensing Technical Review Panel. 4
- R6 AEBN recommends that section 295 F subsections (a), (b) and (c) be omitted and that these be replaced by:
- Imposition of special restrictions on the right to trade in an emissions market
 - Suspension of a participant’s right to trade in an emissions market in which time frames not exceeding three months are set
 - Revocation of a participant’s right to trade in an emissions market where all permits and credits can be repurchased by the EPA at current market rates
 - All participants which have had their ability to trade in an emissions market revoked must revert to their emissions being controlled through POEO licence conditions
- Where any action in section (1) has a similar effect to that of the issue arising from a Prohibition notice or revocation of a POEO licence, these actions must be only invoked by the Minister. 5
- R7 AEBN recommends that EPA have clear rules and restrictions on its ability to trade in an emissions trading scheme which it operates including:
- The EPA must be given clear restrictive rules governing the general trading of permits and credits
 - Preparation of a ten year plan, with the regulations specifying the annual rate uptake or issuance of tradeable permits or credits

- The EPA be restricted to purchasing only enough permits to meet the annual requirements in the ten year plan, except when managing the forced exiting of a player from the market. 6
- R8 AEBN recommends that the total costs of running any emissions trading scheme should not exceed 10% pa of the market turnover. 6
- R9 AEBN recommends that section 295H (a) be redrafted to:
 “require a person to continue to make a contribution referred to in this section in respect of a tradeable emission permit or credit that has been suspended.” 6
- R10 AEBN recommends that the Independent Pricing and Regulatory Tribunal oversee and set price determinations for the administrative and other costs in running the scheme, and it also investigates the economic impacts of the scheme on licensed sites involved. 7

1. INTRODUCTION

AEBN welcomes well designed and effective tradeable emissions schemes that keep administrative costs to a minimum and result in cost effective environmental outcomes.

The Hunter River Salinity trading scheme is one example of such a success. By controlling only one substance, salt into one well defined environment, the Hunter River the scheme works well. Why, because the environmental harm is well defined and the contribution of harm by the players is virtually equivalent.

AEBN is concerned that more complex environmental issues will be addressed by trading schemes under this Amendment Bill. In order to address a complex environmental issues such as air pollution a trading scheme will need to be complex, which incurs heavy administrative costs. If a simple trading scheme is use it will be very unfair, where environmental outcomes are not achieved or achieved at high cost with little reference to local environmental outcomes.

The EPA has been pushing for a overarching trading scheme since the introduction of the Load Lased Licensing (LBL) scheme in 1998 under the POEO (General) Regulation 1998. LBL has long been criticised by industry as a blunt instrument. Unlike EPA licenses where site specifics and local environmental issues can be negotiated and an agreed set of environmental improvements, LBL assumes the same environmental harm is caused over large regions by the same contaminant. It also assumes that the cost in the reduction in the emission of that contaminant is uniform for industry, which it not. LBL will achieve far more in raising Government revenue and fine tuning measurement techniques than actually reducing harm to the environment. It is also a heavily burden on NSW's large but shrinking manufacturing industrial sites by only applying these additional costs on licensed sites. LBL is closely linked to potential emissions trading schemes and was a necessary first step in the establishment of such schemes.

Over the last year the EPA has been pushing for a Nitrous Oxide (NO_x) trading scheme. AEBN believes that this POEO Act Amendment Bill is the start of this process despite the EPA's own findings showing the NO_x scheme would be unworkable. Introduction of a NO_x trading scheme is not welcomed by industry due to the complexities in assigning emitters to environmental harm. This is far more concerning when considering that motor vehicles emit 82% of Sydney's NO_x would not be subject to the scheme. Bringing in the Hunter Valley Power stations introduces another layer of complexity into the process. How much do they contribute to Sydney's ozone¹ problem? The EPA still has no firm scientific data on this issue, but estimates range from 4% to 20%.

¹ NO_x is not the primary pollutant, it is just a precursor that combined with the right atmospheric conditions and volatile organic compounds (VOCs) (read evaporated petrol and similar substances including emissions from vegetation) generates ozone at ground level. Sydney exceed the World Health Organisations' ozone limits about one hour on 10 to 15 days per year. The primary source of both NO_x and VOCs is the motor vehicle.

The EPA funded and overseen, McLennan Magasanik Associates study of licensed sites found that industrial emissions were at 50% of the cap in the Governments Action for Air Policy, published in 1998. So with a cap on industrial NO_x emissions being so far above the current emission levels, a trading unit in a NO_x trading scheme would be virtually worthless due to an oversupply of emission credits.

AEBN is concerned that the EPA is determined to have its trading schemes without properly considering the costs to industry and determining the environmental outcomes. AEBN invites to Government to reassure industry that this is not the case.

2. CONSULTATION

AEBN and other industry associations have not been informed of the proposed tabling of this Bill in Parliament. This is despite some members being at a meeting less than two weeks ago with the key EPA personnel [who](#) would have worked on this Bill.

3. SECTIONAL ANALYSIS OF THE POEO A (TES) BILL

[295C](2)

(2) A tradeable emission scheme regulation is not repealed by the operation of Part 3 of the *Subordinate Legislation Act 1989*.

(3) A tradeable emission scheme regulation may be periodically reviewed by the Minister as provided for by the regulation.

Section 295C(2) exempts any regulation made under this section from the recurring five year Regulatory Review process. Instead the Bill may be reviewed periodically by the Minister.

AEBN does not support this amendment. A trading scheme can have considerable economic consequences on industry by imposing a reducing number of available emissions credits into a market. In addition, the five year regulatory review process also provides industry with over five years certainty of the extent of any reductions in emission credits permitted on the market. The undertaking of a Regulatory Impact Statement appears to be at the discretion of the Minister and not a mandatory requirement as required under Part 3 of the Subordinate Legislation Act 1989.

R1 AEBN recommends that any tradeable emission scheme regulation be subject to the full Regulatory Review process including a comprehensive Regulatory Impact Statement, public participation and five year repeal and review process.

[295D] Licence conditions

(1) The regulations may, for the purpose of giving effect to a tradeable emission scheme, impose conditions on licences.

(2) Conditions of a licence that are imposed by the regulations for the purposes of this Part cannot be substituted, omitted, amended or revoked by a regulatory authority.

(3) To avoid doubt, there is no appeal under section 287 against a condition that is imposed on a licence by the regulations.

(4) This section does not prevent conditions with respect to a tradeable emission scheme from being attached to a licence by an appropriate regulatory authority in the manner provided for by Chapter 3.

AEBN has a major concern with the civil liberties associated with the removal of appeal rights on EPA licence conditions. Should unfair or even damaging conditions be attached to a licence subsection 2 and 3 do not allow rectification without repealing the subsections of the Act. This sets a dangerous precedent.

AEBN suspects the Government may be concerned that variations to the licence conditions made through appeals may weaken the structure of a trading scheme. It undermines the principles of the separation of powers by removing the Land and Environment Court to make reasoned decisions on appeals to licence conditions. A judge will take into account the necessity to ensure uniformity applies, otherwise unfair commercial advantages would be issued.

R2 AEBN strongly recommends that subsections (2) and (3) be omitted and all appeal rights on EPA licences for the purposes of the tradeable emissions scheme regulations be included.

[295E] Imposition of Penalties for Contravention of scheme

Payment of penalty rates is generally preferred by industry over the use of prosecutions. AEBN supports the need for a disciplinary mechanism to penalise unfair play in the market.

AEBN has been opposed to the setting of heavy interest rates against non-payment or late payment of fees and levies. While not condoning the Australian Tax Office's high interest rates of 20% for late payment of tax, NSW environmental laws "*simple interest calculated at the rate of 5% per fortnight*" smacks of usury.

R3 AEBN recommends that any late payment or error done in good faith should not be subjected to penalties and be consistent with section 295K which exempts the EPA from liability.

R4 AEBN recommends that any penalties should not incur interest rates exceeding that of the Australian Tax Office.

Section 295E subsection 3 holds the EPA as the determining authority in estimating the "*quantity of pollutant emitted.. in contravention of the scheme*". This subsection surprises AEBN as it appears to obviate the purpose and intent of the Load Based Licensing Technical Review Panel (LBLTRP). Surely an independent check should be included in the assessment of such indeterminate financial penalties. The LBL TRP is an ideal instrument to ensure independent assessment of penalties set.

The Protection of the Environment Operations (General) Regulation 1998:

42 Functions of Review Panel

- (1) The Review Panel is to advise the EPA concerning the current or desirable contents of such load calculation protocols as the EPA may refer to the Review Panel.
- (2) The Review Panel may also advise the EPA on such other matters in connection with licences as the EPA may refer to the Review Panel.
- (3) For the purpose of providing any such advice, the Review Panel may seek, receive and consider submissions from interested persons and may gather relevant information from any source.

R5 AEBN recommends section 295E(3)(a) and (b) be amended to :

(a) the quantity of pollutant emitted by the participant in contravention of the scheme, as estimated by the EPA and agreed to by the Load Based Licensing Technical Review Panel.

(b) the amount of monetary, financial or other economic benefits obtained by the participant as a result of contravening the scheme, as estimated by the EPA and agreed to by the Load Based Licensing Technical Review Panel.

[295F] Other Action that may be taken by the EPA

Under this section the EPA may also cancel or suspend or order forfeiture of tradeable emission permits. Such action has the power to terminate the operations of a site. AEBN considers such action equivalent as revocation of an EPA licence, and in effect it is a removal in part of an EPA licence.

This is contrary to section 101 POEO Act 1997 which only provides the Minister with the power to issue a Prohibition Notice. Under a trading scheme where critical emissions to that site's operation are under tradeable permits, cancellation, forfeiture or similar can be equivalent to invoking a Ministerial Prohibition notice.

Under subsection (2) action by the EPA to suspend or cancel or require forfeiture of trading permits can be acted upon as the result of "*one or more contraventions of the scheme*". The only comparative powers permitted in the POEO Act is that of Section 82 **Minister May Suspend or Revoke licence if holder convicted of major pollution offence**. The major difference is that not adhering to a trading scheme appears to be a civil not a criminal matter. Even then all major pollution offences must go through the EPA's Board for approval. All these checks and balances appear to be missing or deliberately avoided from this Bill.

Penalty practices which prevent participants from trading in an emissions trading scheme, need to be given reassurances that their site operations will not be affected.

For example a company that due to various reasons has its ability to trade or use the trading scheme terminated. By default the company should have their emissions governed by the

reapplication of licence conditions, either existing or newly negotiated, so to enable the company to continue to operate. Purchase by the EPA of the permits they hold should be undertaken at current market rates. While they may not lose financially the action of placing the company back on to licence controls should be a deterrent. If this is not a deterrent then the tradeable emissions scheme must be flawed offer no advantage over current licence controls.

In any event failure to meet market rule should never receive the equivalent of revocation of an EPA licence. As environmental harm has not occurred, merely a breach of market rules

Repurchasing of tradeable permits from participants which have their rights to participate in a tradeable emissions scheme revoked, must be undertaken at market rates, Permits are property and actions to cancel or forfeiture would invite action for compensation for loss of property and damages. There are constitutional rights regarding the confiscation of private property by Government.

R6 AEBN recommends that section 295 F subsections (a), (b) and (c) be omitted and that these be replaced by:

- ***Imposition of special restrictions on the right to trade in an emissions market***
- ***Suspension of a participant's right to trade in an emissions market in which time frames not exceeding three months are set***
- ***Revocation of a participant's right to trade in an emissions market where all permits and credits be repurchased by the EPA at current market rates***
- ***All participants which have had their ability to trade in an emissions market revoked must revert to their emissions being controlled through POEO licence conditions***

Where any action in section (1) has a similar effect to that arising from the issue of a Prohibition notice or revocation of a POEO licence, these actions must be only invoked by the Minister.

AEBN considers that the rules of any trading scheme should be less than that of current pollution laws under the POEO Act or other relevant laws.

Please also note that the repurchases of tradeable permits will not violate the ten year plan of that has been previously mentioned. While these permits are out of the system the total amount of emissions permitted has not generally changed as the ousted player will still be permitted to operate, unless he breached POEO licence conditions.

In summary AEBN considers that the trading scheme should be a benefit to industry, and participation worthwhile and better than using licence conditions. Consequently the use of penalty actions under a trading scheme should be limited to the ultimate action of removing one's right to trade. POEO licences and other environmental law already has powers to remove and prevent a site's operation along with considerable penalties that can be imposed.

[295G] Participation in the scheme by the EPA

AEBN is concerned about the EPA trading in the market. Clear constraints and rules must be imposed on the EPA's use of its market power and insider information. How can this be done and who will regulate the EPA?

R7 *AEBN recommends that EPA have clear rules and restrictions on its ability to trade in an emissions trading scheme which it operates including:*

- *The EPA must be given clear restrictive rules governing the general trading of permits and credits*
- *Preparation of a ten year plan, with the regulations specifying the annual rate uptake or issuance of tradeable permits or credits*
- *The EPA be restricted to purchasing only enough permits to meet the annual requirements in the ten year plan, except when managing the forced exiting of a player from the market.*

[295H] Cost recovery

Cost recovery goes to the very heart of AEBN's concerns in relation to the efficiency of the trading schemes that are proposed and implemented by the EPA. Already foreshadowed is the difficult and complex nature that a NO_x trading scheme will create. To test the efficacy of a trading scheme the administrative costs must be a small portion of the total market, generally less than 10% of turnover. I know of no stockbroker that charges more than a 10% commission, and that is with liability on use of his advice.

R8 *AEBN recommends that the total costs of running any emissions trading scheme should not exceed 10% pa of the market turnover.*

Under subsection (5) the regulations may:

“(a) require a person to continue to make a contribution referred to in this section in respect of a tradeable emission permit or credit that has been forfeited until the permit or credit is sold or re-allocated,”

The continuous application of market fees is flawed and must have clear boundaries. AEBN considers that only suspended participants from the market should attract such fees. The only other action which AEBN supports is the revocation of the right to trade in a scheme. However, AEBN has stated that the EPA must repurchase all permits and credits at market rates

R9 *AEBN recommends that section 295H (a) be redrafted to:*

“require a person to continue to make a contribution referred to in this section in respect of a tradeable emission permit or credit that has been suspended.”

[295I] Tradeable Emissions Scheme Fund

The intent of the Tradeable Emissions Fund is clear in at least one direction. It can be used to reduce the market size of emission permits by buying them on the market. AEBN has no issue with such practice as long as the buyback rate has been clearly established and on a 10 year cycle.

Overall the scheme is a new style of venture for the EPA. It is now entering the services market and offering a public service to industry on a monopoly basis. As raised previously the issue of who should regulate the EPA on its operation and costs associated with this new service needs to be explored.

AEBN sees little difference between other Government Trading Enterprises and the EPA's proposed trading scheme. The NSW Government has a well respected body to over see the efficiency of such Government activities, even including the Taxi industry. AEBN believes the Independent Pricing and Regulatory Tribunal could fill the role of overseeing the activities of the EPA's proposed trading schemes.

R10 AEBN recommends that the Independent Pricing and Regulatory Tribunal oversee and set price determinations for the administrative and other costs in running the scheme, and it also investigates the economic impacts of the scheme on licensed sites involved.

[295K] Liability for operation of scheme

Section 295K negates liability of the Government on the use and operation of any trading scheme under the POEO Act. While there is some justification for limiting the Crown's liability, there are other matters lacking in the probity process regarding the Tradeable Emissions Schemes Fund.

Clarification of what happens to funds derived from tradeable permits once the trading scheme is dissolved. AEBN considers that the account funds should be divided and the holders of the permits be reimbursed. Permits will be considered property of the holder and like a bond bought from the Government, it should retain its worth according to market forces.

Another issue is the market size in a tradeable scheme. Closure of a major emitter will force the price of permits down in the short term. This is where the 10 year setting down of the amount of permits that will be in the market is important. Otherwise the Government may purchase these permits to keep the price level. In reality the environmental outcome is the reduction in industrial emissions which will be replaced by motor vehicle or other diffuse sources of emissions.

Industry must be able to compete on a level playing field, but with a restrictive emissions cap progressively screwed down on fewer industrial sites, it is a losing game for the licence holder. The outcome will be less industry, lower employment, especially in the higher paid

jobs and similar air pollution levels as the motor vehicle and other emission sources outside the trading scheme will continue to grow with no similar constraint.

4 CONCLUSION

A redrafting of the POEO A (TES) Bill to include many of its omissions of checks and balances will assist NSW in producing a quality foundation for tradeable emissions schemes.

As a result of fairness and good redrafting cost effective and efficient use of trading schemes will be another tool for Government and industry to use to achieve real environmental outcomes. It will also avoid mistakes where jobs are shed unnecessarily as a result of non-environmental breaches of a trading scheme.