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# **SUBMISSION ON IMPLEMENTING THE CARBON TAX**

## **FROM THE GREENHOUSE POLICY COALITION**

## 1. Introduction

- 1.1 Thank you for the opportunity to make a submission on the consultation paper *Implementing the Carbon Tax*, published May 2005.
- 1.2 The Greenhouse Policy Coalition (GPC) represents companies that are the powerhouse of the New Zealand economy across most of the sectors; including manufacturing, steel production, building, cement, agriculture, pulp and paper, coal, aluminium smelting and gas infrastructure networks. They are significant employers, collectively employing approximately 24,000 people in 2003, with an estimated further 79,000 people employed indirectly as a result of these companies' activities.
- 1.3 As large energy and fuel users and large employers GPC members have a strong interest in ensuring Government's policies and measures on climate change are consistent with sustainable economic growth for New Zealand, while contributing to global emission stabilisation and reduction efforts over time.
- 1.4 Greenhouse Policy Coalition member companies<sup>i</sup> generated sales worth \$17.3 billion in 2003 (GDP for 2003 was approximately \$130 billion). They are responsible for generating 27% of New Zealand's exports, worth \$8 billion.

## Chapter 2: WHY A CARBON TAX?

- 2.1 Why a carbon tax is a good question to start with. The Greenhouse Policy Coalition does not believe a carbon tax is the best policy instrument with which to reduce New Zealand's greenhouse gas emissions. We believe that more positive incentives would achieve similar or better results, without the economic drag on the economy of a new tax.<sup>1</sup>

### *Carbon Tax will not reduce emissions*

- 2.2 The carbon tax is unlikely to have much impact on the emissions of greenhouse gases from New Zealand because our emissions are dominated by agricultural and transport emissions where there are no quick fixes. With 49%<sup>2</sup> of our emissions coming from agriculture and 19% from transport, a carbon tax will not have much impact on reducing our increasing greenhouse gas emissions. Unlike other industrialized developed nations, most of our emissions do not come from our electricity generation or our industry. The electricity sector is already dominated by hydro and is 70%<sup>3</sup> per cent renewables when you add in wind, biofuels and geothermal. Thermal electricity generation accounts for only 8%<sup>4</sup> per cent of greenhouse gas emissions and industrial and manufacturing accounts for only 13 per cent of greenhouse gas emissions.
- 2.3 Being geographically widely spread, New Zealanders rely heavily on motor vehicle transportation. A tax on fuel would have to be very high to change behaviour away from motor vehicle use, as we do not have good public transport options throughout the country or the population base to easily fund them.
- 2.4 It is our understanding that the original purpose of the carbon tax was to be a tax to change behaviour. Moving the point of obligation for the tax as far up the supply chain as possible might make for greater administrative ease, but it breaks any link between the tax and changing behaviour. A tax has very little chance of influencing behaviour if it is invisible to the end user and they have no alternatives anyway. The tax will not be explicit like a GST on the end consumer's bill. The cost of their electricity and fuel will simply increase. If they do want to minimise their exposure to the tax and chose 'greener alternatives' what choices do they have? You can not pull up at a petrol station and fill up with gas or biofuels at

<sup>1</sup> NZIER estimate a reduction in economic activity of \$47 million per annum from 2010. NZIER working paper 2005/02, June 2005.

<sup>2</sup> 2003 greenhouse gas emissions, Annual Report on Climate Change Policy Implementation 2004/05, pg 5.

<sup>3</sup> New Zealand Energy Data File, Ministry of Economic Development, January, 2004, pg 107.

<sup>4</sup> 2003 greenhouse gas emissions, Annual Report on Climate Change Policy Implementation 2004/05, pg 5.

present in New Zealand. Anyone purchasing electricity gets whatever is in the mix at the time of dispatch. The carbon tax does not make electricity from renewables more attractive, it just makes electricity more expensive, with windfall gains going to renewable generators when our electricity generation system is already dominated by renewables.

- 2.5 Only if the carbon tax suppresses or cuts demand will there be a swift reduction in emissions. And if this happens our standard of living will be severely cut back, and imports will necessarily increase from countries that are more competitive than New Zealand because they have failed to put costs or caps on their own greenhouse gas emissions.

### *Universal carbon tax a World first*

- 2.6 Although the consultation paper refers to other countries that have imposed carbon taxes, we believe New Zealand is in a small minority. The International Energy Agency's 2003 Review on Energy Policies of IEA Countries states *Fiscal measures are an important part of the policy mix developed by IEA member countries to reduce greenhouse gas emissions, representing almost one-third of all new measures taken or planned in the past four years. To date the vast majority of fiscal measures have been set up to support the development of emerging low carbon technologies rather than to impose direct cost on fossil fuel sources.*
- 2.7 While four European countries have chosen to introduce a limited tax on CO<sub>2</sub>, many more have evaluated the costs/benefits and rejected a carbon tax. Canada, Japan and Ireland are three much richer economies than New Zealand producing significantly more CO<sub>2</sub> emissions<sup>5</sup> (or similar in the case of Ireland), yet they have rejected carbon taxes. None of them, it should be added, looks likely to be able to meet their Kyoto Protocol emission reduction targets.
- 2.8 In countries that are participating in the European Union Emission Trading Scheme (EUETS), those installations that are included in the scheme (15,000 firms) vary from country to country and depend on their national allocation plans. The EUETS only covers about 40%<sup>6</sup> of Europe's total CO<sub>2</sub> emissions, generally only applies to larger installations (industrials and electricity generators) and is only based on the marginal emissions over and above an installation's emissions allocation. In New Zealand the proposal is to tax **each tonne** of carbon, which is a much more onerous proposition.

<sup>5</sup> World Resources Institute, Climate Analysis Indicators Tool. 2000. [cait.wri.org](http://cait.wri.org)

<sup>6</sup> EurActive.com – EU News, Policy Positions & EU actions online, published 21 April 2005.

- 2.9 In addition, you have the countries that are trading and competing with New Zealand, such as the USA and Australia, that are large greenhouse gas emitters and have rejected Kyoto Protocol emission reduction targets altogether. They are choosing to tackle greenhouse gas emissions through other policies and measures, including significant investment in new cleaner technology options. It is frequently overlooked in climate change policy circles, but the USA is investing more on R & D to develop new technology to reduce emissions than the whole of Europe.
- 2.10 Then you have the developing countries, some of which are major emitters and major developing economies, such as China, India and most of Asia, whose refusal to limit their emissions of greenhouse gas or put a cost on them is going to cause immense problems to countries that do. We face losing our competitive advantage and creating leakage of emissions (and industry) from New Zealand, when many of our large industrials are operating close to or at Worlds Best Practice in emissions intensity already<sup>7</sup>. While NGA policy is a necessary part of the policy mix to prevent leakage occurring, there are still many uncertainties around how successful this policy will be in achieving its goal. The fact the NGA policy only gives certainty to 2012 is too short a time frame to give adequate investment certainty to businesses in the energy intensive sector, where investment typically requires long lead times, large amounts of capital and the investment is in long lived assets.
- 2.11 For a country that produces 0.2% of global CO<sub>2</sub> equivalent emissions<sup>8</sup>, choosing to introduce a carbon tax that will cost our economy, potentially slow economic growth and investment and fail to reduce our greenhouse gas emissions, seems to be questionable policy. The Greenhouse Policy Coalition believes there are other policies and measures that could better control emissions growth and be far less costly to our economy.

### *Recycling of carbon tax*

- 2.12 The proposition that the carbon tax will be recycled to business and in effect make the carbon tax 'revenue neutral' is stretching credibility we believe. It has been well commented on by tax advisors in leading CA Firms that increased depreciation on short life assets is not a tax reduction rather the same tax is collected, just over a different timeframe and it will be unlikely to have a material impact for many. The changes are largely

<sup>7</sup> Early indications from WBP studies being carried out as part of NGA negotiations indicates many of our large industrials are already close to WBP in emissions intensity.

<sup>8</sup> World Resources Institute, Climate Analysis Indicators Tool. December 2003. This calculation does not include CO<sub>2</sub> absorption by forests and allows for the different warming potential of each of the greenhouse gases. There is no more recent compilation of Country statistics. NZ's proportion has decreased slightly by 2002.

recognition that for short-lived assets, the historic rates were too low given the speed at which they depreciate. The selected coverage will arguably contribute little to the desired emission reductions. The Greenhouse Policy Coalition was disappointed that long lived large capital investments were not given more favourable depreciation treatment, which would have the positive effect of incentivising earlier up-take of newer and more energy efficient plant and technology which would contribute to a reduction in CO<sub>2</sub> emissions.

- 2.13 In the Confirmation of the Preferred Policy Package (POL (02) 143), feedback from consultation then showed a strong demand for revenue to be used for mitigation, adaptation and other climate related activities. We believe the “recycling” of the carbon tax has failed people’s expectations in this regard and is a missed opportunity to have contributed to emissions reductions.

### *SME Policy*

- 2.14 We believe the policy for the small to medium business sector (which will be unable to obtain relief from the carbon tax because they do not meet the NGA criteria or because the transaction costs of obtaining an NGA are too high) – are inadequate. This will have a significant negative impact on the whole economy.
- 2.15 \$4.45 million being allocated over three years for pilot programmes on energy efficiency for energy intensive businesses in the SME sector is a drop in the bucket (particularly when you consider the carbon tax will raise in excess of an estimated \$400 million per annum). The allocation is equivalent to 0.37% of the tax revenue. Additionally it is not going to assist those that are already energy efficient to cope with an additional tax on their business. We do not believe a rigorous cost/benefit analysis has been satisfactorily carried out on the impact the carbon tax will have on business that is not eligible for NGA’s. It is not just the direct cost of their fuel and electricity increasing; it is all the increasing costs of all their suppliers also impacted by the carbon tax. If the impact of the tax on business is compared with the emissions they produce (8%<sup>9</sup> of NZ greenhouse gas emissions are from manufacturing and construction) it seems akin to using a sledgehammer to crack the wrong nut.

### *NGA’s*

- 2.16 As mentioned above, NGA policy is supported by the Greenhouse Policy Coalition as a way to achieve energy intensity emission reductions and to

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<sup>9</sup> 2003 greenhouse gas emissions, Annual Report on Climate Change Policy Implementation 2004/05, pg 5.

prevent leakage of our energy intensive industries from New Zealand to other countries that do not impose price-based measures. However, for the NGA policy to be successful we do believe that the cost and process of obtaining an NGA needs to be addressed. We are hopeful the review of NGA policy will achieve some better results in terms of processing NGA's and we are working closely on this with the Climate Change Office.

### *Emissions Forecast blowout*

- 2.17 It is of great concern to the Greenhouse Policy Coalition that the revised estimates of our emissions growth to 2012 is now putting us in a deficit position for the first commitment period of the Kyoto Protocol. We understand that a contingent liability associated with our Kyoto Protocol commitments will be placed in the Crown accounts for the first time from 1 July 2005.
- 2.18 The miscalculation of what our commitment to the Kyoto Protocol will cost New Zealanders requires an urgent and thorough review of New Zealand's climate change policies and measures, including the carbon tax.
- 2.19 New Zealanders, and Ministers of the Crown, need to have a better and clear understanding about the costs/benefits and effectiveness of various policies in order to make the trade-offs that need to be made if we are going to reduce our emissions and continue to grow our economy and improve our standard of living at the same time.
- 2.20 The Greenhouse Policy Coalition believes that with an emissions profile akin to that of a developing country (with 49% of our emissions coming from agriculture), with a growing economy, with an energy future that is only going to be more carbon intensive rather than less (according to most credible forecasts) and with a need to plan for secure energy supplies in the future, the options to reduce emissions in New Zealand are going to be limited. The alternatives include restricting growth and development. This needs some thorough and credible analysis so that the costs of action are well understood and the trade-offs that have to be made are put before the public.
- 2.21 While New Zealand needs to contribute to global efforts to reduce emissions and use our energy as efficiently as we can, we need to be pragmatic about how much we can achieve in the absence of new technology breakthroughs when half our country emissions are from agriculture. Introducing policies that will incentivise emission reductions and encourage new technology uptake will be important.



- 2.22 We are not confident that the Permanent Forest Sinks policy will be very attractive as an investment and believe it will do little to stem the deforestation and land-use change that is occurring now.

*Post 2012*

- 2.23 The emissions forecast blow-out for commitment period one of the Kyoto Protocol points to major challenges ahead for New Zealand in future commitment periods when targets are expected to get harder. For all the reasons stated above, we believe that the only way New Zealand will be able to reduce emissions (in the absence of significant technology advances in transport and agriculture) will be to restrict growth. In the absence of a broad global commitment to reduce emissions from both developing and developed countries, New Zealand will need to be very cautious about making future commitments for harder targets. This needs some careful analysis to work out how New Zealand can contribute to the global effort, but in proportion to our emissions and our emissions profile. For example, it might be more appropriate to put New Zealand in a group of countries with a similar emissions profile, such as Argentina, rather than the so called “developed countries’ or Annex 1 countries where the majority of the emissions are from industry, the transport and electricity sectors.



### **Chapter 3: PUTTING A PRICE ON GREENHOUSE GAS EMISSIONS**

*(the following points relate directly to the consultation paper)*

- 3.1 The rate of the tax is a concern already, given the price of carbon in the only cap and trade market (EUETS) has been consistently going up rather than down, and in the first six months of the life of the market has topped €28.85 or over NZ\$50.00 tonne/CO<sub>2</sub>-equivalent emissions, which is over triple the starting rate of the carbon tax in New Zealand. The Greenhouse Policy Coalition would strongly urge a consultation process that engages the voting public in an informed debate (informed with economic analysis on what it will mean for business and consumers) before changes can be made to the rate of the tax. While the Government has signalled a cap of \$25.00 per tonne CO<sub>2</sub> until 2012, many business leaders will be watching the international price of carbon and not waiting around to see what will happen in New Zealand post 2012. It sends a depressing message about the cost of doing business in New Zealand in the future, when the same environmental costs will not be imposed in many competing countries. There is also a concern that now New Zealand is forecast to be in a debit position in CP1, the Government will be incentivised to raise more tax than had we been in credit, to cover the shortfall.
- 3.2 Default emission factors. Some of the emission factors shown in Appendix 2 are incorrect, for example soda ash, lime and dolomitic lime. The IRD should liaise directly with the industries concerned to ensure they are right. We are opposed to using the upper end of the range of emission factors. This will penalise those firms that do not get full relief under their NGA and those firms that do not get NGA's.

#### **Pass-through of the tax (pg 13)**

- 3.3 Greenhouse Policy Coalition believes that the tax will be passed through 100% and any other presumptions are flawed. Information we have from our gas and coal members is that the tax will be passed through 100%. This was always the expectation from fossil fuel suppliers and from NGA firms. To assume it will be any less based on some theoretical modelling will only disadvantage NGA firms which will be paying the full cost of the carbon tax, but unable to claim it back if some faulty assumptions are made due to some theoretical modelling. Our market information tells us there is no reason why fossil fuel suppliers will not pass through the tax 100% and that they fully intend to do so. Because of the competitive pressures they face within their industries, there is no rational basis for assuming either gas or coal suppliers can absorb any of the carbon tax. With regard to gas, any rational seller would price their gas close to the international price range. To do otherwise would provide a disincentive

for gas exploration and would be detrimental to security of energy supply and a barrier to the development of a wholesale market.

- 3.4 NGA holders therefore should be able to claim 100% of the tax back. To assume anything other than 100% pass through will penalise NGA holders and make the NGA less effective in the goal of maintaining international competitiveness for the firm that has an NGA.

### *Stockpiles*

- 3.5 The Greenhouse Policy Coalition would not like to see the carbon tax impact on security of electricity supply if the tax is a disincentive to generators to hold sufficient stockpiles of fuel (say coal) and a pragmatic solution needs to be found for this potentially perverse outcome.

### *Exemptions rebates and refunds*

- 3.6 A threshold of a minimum of \$2000 per year seems too low and would not go far in terms of covering administration and compliance costs.

### *Timing and Rebates*

- 3.7 With regard to the evidence that the tax has been paid on a product when claiming a rebate, the tax should be shown on the invoice as a separate item. This would also assist with deducting the tax from income where appropriate. It would also assist in meeting the Government objective of increasing public and business awareness, and changing behaviour.

## **4. ISSUES FOR SPECIFIC INDUSTRIES**

Given the Greenhouse Policy Coalition represents companies from a number of different industries we will leave industry specific issues to them to respond to individually.

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<sup>i</sup> The Greenhouse Policy Coalition represents New Zealand businesses over a range of sectors.

- Carter Holt Harvey Pulp and Paper
- Comalco Aluminium Ltd
- Business New Zealand
- Norske Skog Tasman

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- Pan Pacific Forest Products Ltd
  - Coal Association of New Zealand
  - NGC Ltd
  - New Zealand Aluminium Smelters Ltd
  - Fletcher Building Ltd
  - Fonterra Cooperative Group Ltd
  - Holcim (New Zealand) Ltd
  - New Zealand Steel Ltd
  - Solid Energy New Zealand Ltd
  - Winstone Pulp International