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Customs, Trade and Transport Law e-alert

Carbon pricing for Transport and Logistics

Brief overview

Assuming Parliament passes the appropriate legislation, a carbon permit system will commence on 1 July 2012 in Australia. For the first three years the scheme will be in a fixed price phase, where one permit will equal one tonne of carbon emitted. During this phase, businesses which meet the relevant coverage threshold will have to purchase (and then surrender) as many permits as they need in order to cover every tonne of carbon they emit in that compliance (financial) year. The cost of those permits will be fixed at \$23.00 per tonne in 2012-13, then \$24.15 per tonne in 2013-14, and finally \$25.40 per tonne in 2014-15.

Fixed permits (those purchased in the fixed price phase) cannot be traded or banked and must be surrendered at the end of each compliance year (and new permits purchased at the new compliance year price). In this period, all businesses that meet the relevant coverage threshold will be able to purchase as many permits as they require to fully cover their emissions. For example, if a business emits 27,500 tonnes of carbon in the reporting year, and that business falls under a covered industry and its emissions are covered emissions, then it will need to buy 27,500 permits, a minimum of 75% of which will have to be surrendered progressively throughout the compliance year, and the remainder surrendered by 1 February the following year.

From 1 July 2015 Australia will then move to a 'cap-and-trade' permit system ("flexible period"). This means an auctioning and trading system, which will occur beneath an overall cap on the amount of permits issued each year. Companies may bank and borrow permits. For the first three years of this period (2015-2018) there will be a fixed ceiling and floor on the price of permits, which will be set in 2014. The ceiling will be set at \$20 above the expected international price. The floor will be set for three years, starting in 2015-16 at \$15 and rising by 4% in real terms each year.

A carbon unit will be considered personal property. However, during the fixed price phase, units will not be transferable. This will change as Australia moves to a floating cap and trade scheme. The trading of carbon permits will have a variety of compliance elements, including the need for parties to register transfers, and to set up a register in their name. We will continue to monitor and advise on developments in this area.

Coverage and reforms to the *Fuel Tax Act 2006*

Transport and non-transport emissions from liquid fuels are not covered under the Climate Energy Bill 2011. This is because the Multi-Party Climate Change Committee was unable to agree on how emissions from liquid fuels should be regulated. However, entities using liquid fuels may still be subject to a carbon price through reforms to fuel tax credits or excise. So domestic aviation, domestic shipping and rail transport, off-road transport of liquid and gaseous fuels and non-transport use of liquid and gaseous fuels will be affected.

Under the Fuel Tax Legislation Amendment (Clean Energy) Bill 2011, which will amend the *Fuel Tax Act 2006*, an entity's fuel tax credit ("FTC") entitlement will be reduced by a carbon reduction amount which will mirror the carbon permit price. The FTC carbon reduction will be \$23.00 per tonne in 2012-13, \$24.15 per tonne 2013-14 and \$25.40 per tonne 2014-15. As the scheme moves to a flexible cap and trade system, from 1 July 2015, the FTC carbon reduction will be based on the preceding six month average carbon auction price. As each fuel, when burnt, emits a different level of carbon, the cents per litre reduction will vary depending upon the fuel used.

Importantly, not all businesses will be covered by the FTC reduction in the first two years. The agriculture, fishing, forestry and **heavy on-road transport industries** (defined as over 4.5 tonne gross vehicle mass) will be excluded from FTC reductions. However, the Federal Government intends to apply a carbon price on heavy on-road vehicles from 1 July 2014. We will continue to monitor and advise about this.

Aviation fuels and non-transport gaseous fuels are not eligible for FTCs (and hence not captured by the FCT reductions), and are not covered by the fixed price permit system. They will however still be caught by the new carbon pricing scheme. The tax rates for aviation fuels under the *Excise Tariff Act 1921* will be adjusted by the amount of the notional carbon price to be put on the fuel emissions, as if aviation fuel was subject to a carbon charge. Under the Excise Tariff Legislation Amendment (Clean Energy) Bill 2011, the aviation fuel carbon component rate will be added to the existing CASA levy to achieve a new aviation fuel excise rate.

The Customs Tariff Act 1995 will also be amended (in an almost identical fashion to the above) so that the aviation fuel excise equivalent customs duty rates will include an aviation fuel carbon component rate. Amendments will also be made to the *Customs Tariff Act 1995* to ensure the carbon charges apply to existing Australian Free Trade agreements.

Passing on the costs

Passing on costs (indirect or direct) must be handled with care, but contracts can specifically allow the passing on of the costs of either permits, reductions in the FTC entitlement, or unit shortfall costs.

The passing on of costs should be considered not only by the initial entity that seeks to pass the costs down the line, but also the entity that receives the cost increases. Even if your company does not fall within the coverage threshold, you may be affected through a passing down the line of costs, and should review supply contracts accordingly to ensure you are in the best position to pass on, or avoid, cost increases due to carbon pricing.

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A company will risk breaching the *The Australian Competition and Consumer Act 2010* (Cth) unless it has the documentation and price modelling to prove any price increase is directly related to a carbon price cost. That Act specifically prohibits, via the Australian Consumer Law, misleading and deceptive conduct.

On July 10 this year, the Federal Government announced that it will direct the Australian Competition and Consumer Commission ("ACCC") to give the highest priority to investigating and taking action against corporations and businesses that make false or misleading representations in trade or commerce about the impact of the carbon price on the price they charge.

We can help by reviewing your standard terms and conditions, and other related contracts, to pass on, or avoid the costs, as may be appropriate. We have extensive experience in advising on coverage under the National Greenhouse and *Energy Reporting Act 2007* ("NGER Act"), and are well placed to help you transition to the new carbon pricing reporting requirements and work out whether you will meet the coverage threshold requiring you to purchase and surrender permits.