

Australian Institute of Environmental Accounting Teleconference
Carbon Pass Through Costs Discussion Minutes
11am EST, 9am WST Friday 27th July 2012

15 Attenders:

Name	Company
Clare Ryall	AIEA
Russell Marks	AIEA
Murray Ryall	Greenbase
Shawn Pearson	Citic
Matt Drum	Ndver
Andrew Gunst	AIEA
Karen Boyce	Tronox
Brendan Bateman	Clayton Utz
Peter Davis	Tronox
Chris Doherty	Ernst & Young
Monica Yuen	Greenbase
Andrew Taylor	SCA Hygiene
Angela Ryan	Wesfarmers
Ros DeGaris	DeGaris Consulting
Wayne Rossiter	WPG Resources

Conference Dialogue Summary

Russell Marks (05:40): (1) How much do we add onto the liability when we are passing on the cost e.g. electricity generators/ suppliers? (2) How much do we need to budget for if we cannot pass on the cost such as mining companies? (3) What factors are we considering in order to estimate the on-cost with any examples (i.e. what percentage should be)?

Matt Drum: Using electricity retailers as an example. Most are currently charging 2.168 cents per kwh on top of the energy component. The cost is adjusted with TRS and information is available on AER (Australian Energy Regulator) website.

Transmission and distribution are the considering factors but they vary within regions.

Ros DeGaris: I applied a simple calculation based on electricity at home. A difference has been taken between the old price and the new price of the electricity. Result suggests carbon pass through 30-40% of the increased power with particular supplier. This gives an estimation about the emission over transmission.

The calculation is expressed carbon in kwhr based on state factor and available information in public domain. Cost is expressed in terms of electricity price within 1 July 2011 – 1 July 2012. However, calculation does not take consideration of any administration cost.

Russell Marks: Using an all diesel operation as an example, according to the scope 3 emission, there will be an on cost approximately 7.5% when transport emission is included in the system. If administration cost is considered, the on cost will be higher than 7.5%.

Matt Drum: The administration cost should be zero, or negligible, as the cost will be absorbed by all the customers, using the retailers & supply chain as examples here. However, this case may not apply to mining industry or electricity generators. The cost of administration or association will be spread out and therefore becomes negligible.

The large grid retailers are in scope 2 and the state based national average grid factor / average grid factor is 0.94. This factor can be used for carbon loading on the energy supply.

Ros DeGaris: According to the NGER source, the emission factor for scope 3 is 0.13.

Russell Marks: The supply chain will have to absorb the administration cost by itself. When in the future, when the transport is being taken into account by the scheme, there will be an impact on the supply chain emission.

Matt Drum (14:50): In order to determine the ability of a company passing on the cost to its supplier (e.g. manufacturing industry), it requires some analysis. It requires to break down the supply chain cost (e.g. licensing costs) and value of the contract. The value of contract can be put into 2 categories:

(a) High value, high intensity contract (e.g. chemical supplier) – it requires analysis on their emission profile, EPA system, onshore activities versus offshore activities. For example, the energy cost which can be passed through will depend on the onshore operation in the future. This can eventually estimate the energy cost and give operational expenditure estimation.

Cost which is not energy related will be multiplied with the CPI and gives 0.7% increase in 2015 & 0.2% increase in 2015-2016. They are the flexible price periods. The cost of a product can possibly increase by 3%.

(b) Low value, low intensity contract (e.g. service provider) –it varies with the scope. The budget is usually applied to the treasury modelling and to estimate the percentage increase. For example, a large chain supplier can pass through their cost by 1.7%.

Russell Marks: A study suggested the cost pass through can reach 11% but it is a bit too high. The impact varies with business and individual case is different from one another. Therefore, it requires a detailed business analysis.

Karen Boyce (22:10): One of the clients has a large electricity cost and the electricity cost can expect to increase by 20%. Therefore, the passing through is more likely close to 20% than 3%. However, the percentage of pass through varies with company situation.

Russell Marks: we however attempt to look for a reasonable percentage pass through that could apply to mining companies.

Karen Boyce: In mining perspective, diesel cost should increase no more than 7-9%. Therefore, any increase more than the diesel cost can be considered unreasonable or out of expectation.

Russell Marks: All diesel operation cost is expected to be 5-10%.

Karen Boyce: A change in the fuel tax credit however does not mean the rebate become smaller but there will be a cost increase for the companies from using diesel. As previously, transportation is not covered but once the transportation using diesel is included, there will be a cost increase.

The rebate gets smaller and therefore, the cost for companies from using diesel increases, particularly mines sites as they have lower rebate. The overall cost increase shouldn't increase the costs of the diesel.

Shawn Pearson: Using CITIC Pacific as an example, there is a price increase but 20% seems to be a high number but is still an acceptable estimation. However, 20% increase on the electricity price is not driven by carbon price.

Karen Boyce: 20% is particularly applied on those companies which base in WA and those who have low electricity price only. Once the carbon price is introduced, and it is a fixed cost, the carbon price will seem to become a large proportion of the total cost.

Andrew Gunst: 20% is still considered as a reasonable estimation. However, the challenge of the estimation is whether it is a fixed cents per kwh increase or fixed cent per litre of diesel.

If it is for non-transport purposes, the particular case for electricity viewed as percentage and those who have a low-price contract, there could be a 40-50% electricity price increase. Therefore, there will be a chance to negotiate for 4-5 cent per kwh electricity.

Matt Drum: There is not necessarily the case that electricity price will increase by 20% and leads the price of the goods to increase by 20%, associated with the carbon price. The electricity cost is only a portion of the operational expenditure.

In order to determine how much the price of the goods should be increased by, we need analysis on the actual cost increase on the business and apply to the actual operational expenditure increase. However, this needs to be confirmed by the ACCC about the price increase of the goods driven by the carbon price, providing quantified evidence.

Ros DeGaris (28:50): Does anyone have any knowledge about the cost pass through about things like steam or co-generation?

Matt Drum: It will base on its emission and liable entity. First assume the emission above the threshold and the amount of emission will then be multiplied by its emission factor.

Karen Boyce: BP in WA can be used as an example here and since they have co-generation facilities, they may have some insight for that.

Andrew Gunst: The challenge for co-generation still remains as there is an attempt to allocate the cost to the steam. It is a marginal cost allocation which is hard to divide into percentage increase. Therefore, it will need to refer to the ACCC documentation to support any statements. However, certain information in public domain can help determine percentage split.

Karen Boyce: NGER measurement determination is a good guide for the percentage split to allocate emission for the electricity.

Andrew Gunst: Yes, that's a good idea.

Brendan Bateman: Measurement standards can however vary with circumstances. Hard to find a reference point and then you would need to decide if that reference point can be adopted to your situation.

Andrew Gunst: That makes sense, the challenge in a co-generation plant is day to day you might move that ratio, establishing the real split can be quite challenging.

Ros DeGaris (32:16): Does anyone know where can an emission intensive trade expose industry get assistance from not being successful to pass through cost?

Andrew Taylor: We have a supplier who has assistance and does not pass through cost to our organisation saying they are not legislated or required to. They are diverting the assistance carbon abatement exercises elsewhere in their organisation. Our experience is they are passing through what they determine to be the full carbon cost and they 94.5% assistance they get they are not passing through.

Brendan Bateman: it depends on the contract condition if pass on cost is contained in the supply contract, in most cases, they will receive assistance. However, this underlies the market price of the goods is acceptable and its actual liability. In other words, they become legally contractually obliged.

Andrew Taylor: There is a carbon pass through clause in the contract allowing a cost pass through but the calculation wasn't specified and how that would be transferred. Meanwhile, it will need a detail breakdown for its non-emission activities. A calculation result shows the actual intensity liability is about 0.4-0.5%.

Matt Drum: Did you experience any resistance to find out the pass through regarding information provided.

Andrew Taylor: They are actually very proactive. They provide lots of information about natural gas generation, logistics airline, raw material.

Matt Drum: There is a published article about suggesting high carbon intensity should not have any pass through.

Shawn Pearson: Can log in a productivity review to the government and the government will need feedback from the supplier and then to evaluate the level of assistance provided for the cost pass through.

Angela Ryan: However, some non-trade expose products that they made can incur a price increase.

Shawn Pearson (43:30): Regarding to the Liability Transfer Certificate (LTC), an argument can be made here. If you are a liability entity but transferring the liability through a LTC to another entity within your group, whether you are liable to the carbon price within your contract this can make your carbon price increase. If you are not a liability entity, you are not subjected to the LTC process.

Matt Drum: We will also need to look into an issue about the liability and carbon pass through, based on the relationship between the intensity and the transfer.

Shawn Pearson: A problem can be created as a company can generate profit for itself by passing the cost through to the supply chain. Therefore, this will become a competitive commercial decision. Companies can withhold the benefits or profits that they are receiving.

Andrew Gunst: One possible solution is to check the pass through of the industry using published information. For example, Aviation such as Qantas, Virgin has carbon offset information published and they can be adjusted in carbon pricing. It will be a good indicator to check their NGER emission and their NGER emission and can estimate their 97% of their emission is due to combusting jet fuel.

Therefore, we can use a simple calculation to work out the cents or percentage cost pass through. We can also work their dollar per round. This will be useful information for what the industry can charge for their service or product.

Clare Ryall (47:25): This is an ongoing discussion and we would like to hold a panel discussion at the AIEA conference in November. If anyone is interested in being on the panel, please contact the institute via email.