

Smart Business in Action
Sustainable Business Australia
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**The Conservation of Natural Capital
for a Healthy Environment and a Productive Economy**

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What does it mean to be a truly sustainable society?

A truly sustainable society is one that creates wealth without degrading its natural capital.

The conservation of natural capital is, or at least should be, a universal human value that underpins all political philosophy. The great US Republican President Theodore Roosevelt once said: *“Of all the questions which can come before this nation, short of the actual preservation of its existence in a great war, there is none which compares in importance with the great central task of leaving this land even a better land for our descendants than it is for us.”*

This means maintaining our environmental assets in a healthy condition, so that they can provide the goods and services that underpin our economy and improve the wellbeing of people.

The Australian Treasury describes wellbeing as the total stock of capital – human, physical, social and natural – that is maintained or enhanced for current and future generations. It relates to all aspects of life, and encompasses much more than simple measures of economic activity. It means maintaining a stable climate system, it means maintaining our soil and rivers and estuaries and forests and oceans in a healthy condition, and it means protecting for all time those precious gifts of nature – our natural heritage.

The test is not how much we use, it’s whether our use degrades these assets.

I’m going to talk to you about the paper the Wentworth Group released in consultation with experts in economics, land use planning and law in November last year: *Blueprint for a Healthy Environment and a Productive Economy*, and another more recent publication titled *Using Markets to Conserve Natural Capital*. Both papers are available on the Wentworth Group web site: <http://wentworthgroup.org/wp-content/uploads/2014/11/Blueprint-for-a-Healthy-Environment-and-a-Productive-Economy-November-2014.pdf>

<http://wentworthgroup.org/wp-content/uploads/2015/06/Wentworth-Group-Blueprint-Technical-Paper-1-Using-Markets-to-Conserve-Natural-Capital-June-2015-FINAL.pdf>

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In these papers we describe the magnitude of the environmental challenges Australia faces, we establish the case that it is possible to grow the economy and protect the environment, and we set out five long-term institutional and economic reforms that we believe are essential to achieve this outcome.

As we all know, even in the best of times, tax reform is difficult, and given the other pressures on deficits and demographic pressures such as the aging of the population, and in a world where short term reigns, long term management of natural capital is not a high priority.

In reality, the only way we will get long term economic reform to address long term environmental challenges is if a) such reforms are built into broader public policy reforms; and b) we show this they can be achieved without a significant call on the budget. A key objective of our papers is therefore to demonstrate a credible economic case that it is possible to grow the economy, create jobs, (actually cut taxes if that's our desire), and do so in a manner that would also lead to the long-term conservation of our nation's natural capital.

We did this because a generation of Australians have not had the conversation that we can grow the economy and have a healthy environment – they only hear that we must sacrifice one to have the other.

Wentworth Group are not economists, so we were delighted that people such as Dr Ken Henry (former Treasury Secretary), Professor Quentin Grafton (Crawford School) and Martijn Wilder (Partner at Baker McKenzie), agreed to contribute to our blueprint.

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Having established the case that it is possible to grow the economy, create jobs and have a healthy environment, we set out the 5 major long term institutional and economic reforms that are necessary to achieve this outcome. Let me briefly sketch out some of the main elements underpinning each of them:

1. Fixing our reactive land and water use planning systems. Not only is bad land use and infrastructure planning a drag on economic growth - delays and uncertainty in development approvals, congestion in our cities, and unnecessary damage from extreme weather events, it is also the driver of long-term environmental degradation because it fails to take into account the cumulative impact of development on environmental assets.

2. Using markets to finance conservation: Our proposition is a simple but fundamentally important one: remove subsidies from activities that pollute the environment and create economic incentives for business and consumers to restore and maintain environmental assets that have been degraded in the past.

One way of doing this is to eliminate fossil fuel subsidies and tax expenditures that are costing the rest of the economy in the order of \$8 billion a year, and use some of these savings through an equitable, broad-based land tax to pay farmers, indigenous communities and other landholders to restore degraded environmental assets.

This second option would not only result in less tax on the rest of the economy, it would also go a long, long way, in combination with a price on carbon, to restoring and maintaining the nation's natural capital long into the future.

3. relates to **Conserving natural capital** by closing the gaps in our public and private reserves, connecting these across the landscape, and committing to a long-term plan to conserve our native plants, animals and ecosystems.

In doing so, we will also create wealth and employment opportunities for more people, because access to nature in an increasingly congested world, will be valued more highly, and will attract growing numbers of international visitors.

4. Regionalising management of Australia's natural resources so that investment decisions are underpinned by an understanding of how landscapes function.

It will also drive massive efficiencies in government. I can tell you from personal experience, there is enormous scope for reducing duplication and improving the efficiency across all three levels of government.

We are not proposing a fourth tier of government. What we are advocating is that we streamline these institutions so that everyone, investors, government, farmers and other private landholders, are all heading in the same direction.

5. Fundamental to all of these is **creating a system of national environmental accounts.**

In the context of this broad suite of long-term economic and institutional reforms, let me focus on two of these proposals: using markets to finance conservation by removing subsidies that pollute the environment; and establishing a system of national environmental accounts.

Using Markets to Conserve Natural Capital

Our argument for market reform is centered on the understanding that many market activities damage the environment, but this is often not reflected in the market price of the goods or services these activities produce, and as a consequence the cumulative impacts of individual decisions are often masked within the production of goods and services that people consume.

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We argue it is therefore in the public interest for governments to create the economic conditions for these impacts to be incorporated into the cost of doing business, and we identified four opportunities to achieve this:

1. Applying a duty of care, on both private and public land, so that future actions of individuals, businesses and government result in no net long-term harm to the nations' environmental assets;
2. Setting an effective long-term emissions reduction target with a price on carbon to encourage carbon farming to transform the way we farm and manage the Australian landscape;
3. Eliminating fossil fuel subsidies that cause pollution and replacing them with a broad-based land tax to provide a long-term, equitable funding base to pay farmers, indigenous communities and other landholders to restore and maintain environmental assets in a healthy condition; and
4. Developing voluntary, industry-based farm certification, supported by strong and effective regulation, so that suppliers, retailers and consumers can have confidence, and farmers can receive financial benefits for managing their farms sustainably.

Central to these market reforms is that we are able to show:

- a) How a price on carbon can drive continental scale investments in landscape conservation that will make a real difference; and
- b) That by eliminating existing fossil fuel subsidies that cause climate change, and using part of those savings to create incentives to restore degraded environmental assets, it is possible to cut taxes and create a healthy and productive Australia, without any impact on the budget or economic growth.

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Healthy landscapes store more carbon

One of the benefits of a small population living on a large continent is that we have more opportunities to store carbon in vegetation and soils as part of our response to climate change.

The scale of opportunity is enormous. If Australia were to capture 15% of the biophysical potential of our landscape to store carbon, it would offset the equivalent of 25% of Australia's current greenhouse gas emissions, every year for the next 40 years.

In December 2011, the Australian government introduced a carbon offset scheme, the Carbon Farming Initiative. It has the support of all political parties and is one of the broadest and most comprehensive schemes of its type anywhere in the world. Its objectives are to assist in the achievement in Australia's greenhouse gas mitigation obligations in a manner that will protect the environment and improve resilience to the effects of climate change.

Whilst carbon farming has figured prominently in the first round of auctions, CSIRO modeling suggests a price of \$30 tonne is required to leverage landscape scale investments. The first round of the government's Emission Reduction Fund auction set a price of \$14 tonne.

However, if Australia were to adopt emissions targets consistent with a commitment to limit global warming to 2 degrees, the price on carbon is likely to range between \$30 and \$100 per tonne within 10 years.

Once a price exceeds \$30 per tonne, the gross investment potential for landscape conservation could be in the order of \$4 billion per annum if Australia were to capture this 15% of the biophysical potential of our landscape to store carbon. This scale of investment would not only make a significant contribution to Australia's greenhouse emission reductions, it could transform the way we manage the Australian landscape.

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A tax system that conserves natural capital

As I have said, there is no reason why the Australia of today cannot grow the economy, create jobs and maintain a healthy environment. But we have to stop kidding ourselves that the short term decision-making that is pervading our land use decisions today is not having a negative long term impact on our environment, and on our economy.

And we've got to stop kidding ourselves that the small handful of people who are responsible for managing Australia's vast land and water resources – our farmers, indigenous land managers, and managers of our local and national conservation estate, have anything like the resources to do it without financial support from the rest of the community.

We all benefit from a healthy environment. We therefore need to make it profitable for Australian farmers and other land managers to provide these services on behalf of the rest of Australia.

The review of Australia's taxation system presents such an opportunity, and it could benefit from many of the recommendations of the 2010 Henry Tax Review. This review identified a broad set of taxation arrangements that would best position Australia to deal with the social, economic and environmental challenges for the next forty years.

The Review did not conclude that the tax system was broken or in crisis, but it did recommend reform to best position Australia's tax system for the future by addressing issues:

- Australia's overall tax levels;
- The distribution of taxes between the Commonwealth, state and territories and local government;
- Improving the efficiency of the tax system;
- Minimising the effects on economic growth; and
- Ensuring that tax settings do not work against environmental goals.

The starting point for ensuring that tax settings do not work against environmental goals is to phase out subsidies to fossil fuels that create an economic incentive to pollute, in favour of incentives that reward investments in technologies that contribute to protecting the environment.

The WTO defines a subsidy as a financial contribution by a government that confers a benefit. A benefit is conferred when the financial contribution is provided to the recipient on terms that are more favourable than those that could have been obtained from the market.

On the basis of this definition, fossil fuel subsidies and tax expenditures amount to in excess of \$8 billion per annum in Australia. Fuel tax credits alone benefit the fossil fuel sector in excess of \$5 billion: mining (\$2 billion), transport (around \$1 billion), and primary industries (around \$600 million).

A common criticism about the removal of these subsidies is that they are not subsidies because they are inputs into production. There is no case however, in principle, for taxing something more lightly simply because it is a business input. Land is a business input and yet land taxes are the most efficient of all taxes. Labour is the principal input to business, and yet labour is subject to income tax.

A second criticism is that the elimination of these subsidies will cost jobs. Tax subsidies on fossil fuels don't create jobs, they simply mean that there are more jobs in businesses that use a lot of fossil fuels and fewer jobs in businesses that don't use fossil fuels.

Where subsidies are utilised, they should support those industries that will assist in our transition to a low carbon economy, many of which will become industries of the future.

Nowhere is this more obvious than in the support for clean energy, which, by taking advantage of our ability to harness the sun and wind, is now a key part of the global economy and our energy future, bringing with it significant employment growth.

It makes no sense to pay for something that will make us worse off, when for less than half the cost we can pay for something that generates benefits for generations.

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National Environmental Accounts

Finally let me briefly describe the fifth of our five reforms: creating a system of national environmental accounts.

At its most fundamental level, our problem is we measure the benefits of economic growth but that's only half the ledger, because we are not accounting for the depletion of natural capital that some of these economic activities are causing.

This was recognised over 20 years ago at the first Rio Earth Summit in 1992 -*"The first step towards the integration of sustainability into economic development is the establishment of better measurement of the crucial role of the environment as a source of natural capital and as a sink for by-products generated during the production of man-made capital and other human activities."*

It is not possible to manage the economy without economic accounts. Neither is it possible to manage the environment without accounts that measure the condition of the environment.

If you don't measure it, you can't manage it.

If ever you need proof, just look at the Intergenerational Report that was released earlier this year by the former Treasurer. Putting aside the politicisation of what was supposed to be a 5 yearly 'State of the Nation' report Peter Costello originally intended, you will see the extraordinary sophistication in our understanding of the economy and social and demographic trends, but under the heading 'environment' the best the Abbott government could do is repeat is pre-election press releases.

If we are to integrate the management of our environment into everyday economic decisions we need a consistent, comparable, practical and affordable way of measuring the condition of environmental assets at all scales at which economic and policy decisions are being made – whether it is Commonwealth investments in ecosystem services, setting targets for regional NRM investments, or acquiring and managing environmental flows in the Murray Darling Basin, down to farm scale monitoring of their environmental assets.

Many attempts have been made through State of the Environment reporting, which whilst useful, have all failed to produce environmental information that can link to economic decisions.

Over the past 4 years the Wentworth Group has been working with Australia's 56 regional natural resource management bodies, CSIRO, the Australian Bureau of Statistics, state agencies and other experts, to conduct a continental scale trial of what we are calling the *Accounting for Nature* model.

We developed this model with the help of experts in 2008. It provides a framework for measuring and tracking the change in condition of environmental assets, using a common unit of measure based on reference condition.

It can be applied at any scale – national, regional, property or paddock.

When the results are published in a few weeks time, they will shine light on what I believe will be one of the most important policy advances of the 21st century, ... because it means finally, we can use science to address one of the great failures of public policy of the twentieth

century, our inability systematically measure the condition of environmental assets at scales that can inform policy and investment decisions.

It will do for environmental policy, what the national accounts do for economic policy.

I'll take you through some examples to give you a flavour of the power of environmental accounts to underpin a sustainable economy.

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The role for business leaders.

In conclusion, let me address the question: so what specifically can business do?

I'd offer three suggestions. The first two are fairly obvious:

Firstly, the knowledge of these big, long-term environmental trends will increasingly underpin your evaluation of the long-term opportunities and risks to your investment portfolios.

Secondly, you can make a contribution through your own business practices. At the very least if you haven't already, you could identify the many opportunities for your business to both save costs and at the same time reduce your environmental footprint.

The third is a bigger challenge:

I'd be very surprised if anyone here would disagree with the propositions I have put today. You might challenge some of the detail.

The problem I have is the same problem we all face is that the collective actions required to support a growing economy and a healthy environment are far beyond the ability of any individual or company or government to address on their own.

Business leaders do get the problems and they do understand the structural reforms necessary to solve them, but as we know from history, our best chance of success is always when government does these things because our community demands it of them.

When industry sectors group, you do so because it's in your own self interest to do so.

And when you do speak with one voice, you have an enormous influence on public policy.

So my suggestion is this: if you accept that conservation of natural capital is in the long-term self interest of your customers, then it is in the long-term self interest of business for national economic reforms to address the long term decline in the condition of our environment.

So please, work with us to ensure that future economic reforms do lead an economy that not only promotes economic growth, but one that also conserves our natural capital for the long haul.

There is no reason why the Australia of today cannot grow the economy, create jobs and maintain a healthy environment.

And when we do we will *"leave this land even a better land for our descendants than it is for us."*

Thank you.