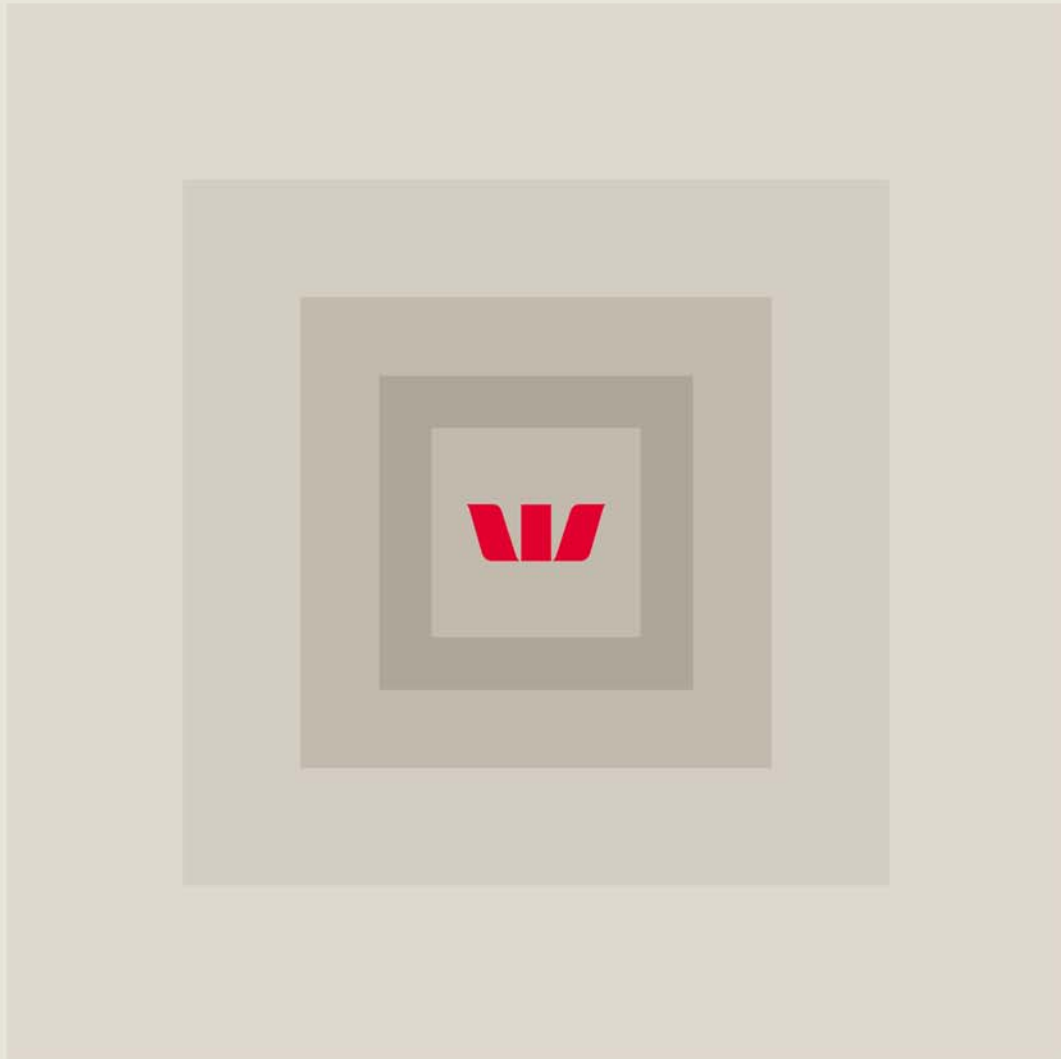


Senate Standing Committee on Environment and Communications



Westpac submission: Inquiry into Carbon Credits (Carbon Farming Initiative) Bill 2011; Carbon Credits (Consequential Amendments) Bill 2011 and Australian National Registry of Emissions Units Bill 2011



Summary

Thank you for the opportunity to make a submission to the Senate Standing Committee on Environment and Communications.

Westpac is well positioned to work with Government on the Carbon Farming Initiative (CFI). Westpac Agribusiness is a market leader with nearly 200 years experience in the sector. Westpac Institutional Bank has been trading carbon in the EU since 2006, undertook the first trade of carbon in Australia in 2008 and is the first and only bank currently making a market in the New Zealand ETS.

The Australian agricultural sector is one of the most efficient and well-managed in the world. Australian farmers, given the volatility of climatic conditions and the natural landscape have become highly experienced at land and water management practices. They continue to innovate in terms of land management practices, with due consideration towards sustainability and environmental best practice.

Establishing an effective and viable policy framework for the origination and certification of domestic offset credits is a key component of the suite of policies required to achieve a 5% reduction in greenhouse gas emissions across the economy.

Westpac's recommendations to the Committee for this Inquiry can be summarized as follows:

- Westpac supports the development of a market and crediting framework which recognizes the role of land sector abatement in meeting Australia's national emission reduction commitments.
- Westpac supports the passing of legislation to establish the Carbon Farming Initiative (CFI).
- Westpac does not support the inclusion of the agricultural sector within the proposed compliance scheme at this stage.
- Westpac believes that there are a number of outstanding issues pertaining to land title and security registration which will need to be addressed in the establishment of the CFI framework.
- Westpac would encourage all Federal, State and Territory Governments to work together to establish an aligned approach to carbon title registration on land title to allow financial institutions to manage the security implications and provide investment support for the growth of carbon origination and reduction projects.
- Westpac would strongly support the eligibility of CFI credits for compliance purposes in any future Australian compliance market, including during the fixed price introductory period.

Westpac has been engaging with customers and industry participants in the agricultural sector for a number of years on the role of market based carbon abatement mechanisms for farmers and landowners, and the implications for both Westpac's funding and financial markets activities.

This submission also draws upon the bank's considerable experience in factoring environmental considerations into business policies, systems, and procedures as well as our practical participation in environmental markets to date.



Submission

1. Westpac position

Westpac is an active participant in ongoing public policy dialogue on the design and operation of a market-based response to climate change. We welcome the opportunity to provide a submission on draft exposure legislation to implement the Carbon Farming Initiative and related enabling infrastructure.

Westpac accepts the scientific consensus on climate change. We believe that climate change will have significant economic, social and environmental impacts in the regions where we operate. Upon examining the projected economic impacts on Australia, we formed the view that a precautionary approach to managing current and future risks is required.

Westpac supports the implementation of a price on carbon and the application of broad based market mechanisms as the most effective, affordable and flexible means of transitioning to a low carbon economy. This must be implemented as part of a suite of policy responses aimed at tackling the various policy and market challenges associated with structural adjustment to a low carbon economy.

We recognize that this will be challenging, and that there is clearly a case for a number of adjustment support mechanisms with the introduction the scheme to allow business and the community to transition into a carbon-constrained economy. Westpac is focused on developing practical products and solutions for our customers to assist in managing the transition to a low carbon operating environment.

Westpac has played an active role in participating to the development of an appropriate policy response for Australia, under both current and previous Commonwealth governments and at the state and regional level. We have worked closely with the Australian Bankers Association (ABA) and the Australian Financial Markets Association (AFMA).

Westpac has also participated in a number of multilateral industry-led initiatives, aimed at promoting a better understanding of the challenges involved in implementing an effective policy response to climate change. This has included the 2006 Australian Business Roundtable on Climate Change (www.businessroundtable.com.au), the 2007 Australian Business and Climate Group review of investment barriers for clean technology (www.businessandclimate.com), the 2008 Australian Agricultural Alliance on Climate Change (hosted at www.climateinstitute.org.au) and commissioned research through Bloomberg New Energy Finance on investment opportunities for clean energy in Australia in 2010. All of which have informed our views.

Westpac will continue to engage with the Government around the design and implementation of the carbon market as the debate unfolds.

2. The Carbon Farming Initiative .

Westpac supports the establishment of the Carbon Farming Initiative (CFI) and believes it will have the following benefits:

- The CFI will provide new sources of revenue and income for farmers and landowners, particularly through generating income from previously untapped marginal land.
- The CFI will provide new sources of revenue and income for Indigenous landowners with consequential social and economic benefits for regional communities.
- The CFI will facilitate greater access to international carbon markets, by providing a framework and certification process for Australian land management and emission reduction projects.



Submission Institutional Bank

- The CFI will establish a credible framework and commercial incentive for the private sector to invest in emissions abatement projects in regional communities to assist in meeting Australia's national emission reduction objectives.
- The CFI will provide a framework for the origination and certification of Australian voluntary credits for use by Australian companies looking to provide offset products and services, or to certify their organization 'Carbon Neutral' under the National Carbon Offset Scheme (NCOS).
- The CFI will provide a pipeline of low cost domestic abatement for liable entities seeking to manage their carbon price exposure over time under a future national compliance scheme.

In particular, Westpac believes that credits originated under the CFI will play a significant role in helping liable entities manage costs under the proposed compliance market within Australia, including during the fixed price introductory period.

The ability for Australian Carbon Credit Units (ACCU) generated under the CFI to be converted to Kyoto compliant credits for export into international markets is a valuable component of the scheme. However, the domestic compliance market will be key to ensuring the commercial viability of investment projects to sequester or reduce emissions across the land use sector.

Westpac believes that it is critical that credits generated under the CFI be eligible for compliance purposes under the proposed emissions trading scheme.

Westpac notes that some organizations have expressed concerns that allowing the use of domestic offset credits for compliance purposes will somehow lessen the incentive for liable entities to invest in emission reduction projects across their own facilities. There are a number of considerations to be taken into account when assessing the likelihood of this occurring in a significant way.

Firstly, there are practical constraints on the number of offset credits which will enter the market in any given year. This is partly because of the length of time it takes to develop a project from establishment to final issuance of credits and partly because of the finite availability of projects suitable for large-scale sequestration activities. Westpac believes that there will be a slow but steady increase in the volume of credits entering the market but that this is unlikely to match the volume of demand required to have a significant impact for liable entities for the foreseeable future.

Secondly, reforestation or sequestration activities, able to deliver a secure stream of offset credits at scale, peak and then fall over time in their ability to deliver a significant volume of credits per project. Westpac believes that it would be more beneficial to consider forestry and land use projects as part of the medium term transitional arrangements able to smooth over the price impacts for industry of costing carbon into investment and operational decisions for business rather than a solution in and of itself.

3. Key design considerations

In reviewing the draft legislation, the following key considerations have formed the basis of our feedback on specific design elements of the CFI. The framework must deliver:

- Certainty of cash flow for carbon projects
- Certainty around security implications for landowners; and
- Certainty of liability for all eligible interests.

These three dimensions underpin Westpac's comments on specific provisions within the Carbon Farming framework.



Key design considerations

Additionality

Westpac supports the application of robust integrity standards to Australian carbon offset credits, which meet or exceed international standards. High standards will increase appetite for credits produced which will in turn lead to the creation of more value.

Westpac notes the importance of a robust and systematic approach to assessing “additionality” for each project. This will be important, not only in meeting crediting and project approval requirements, but also in determining the end market value of the carbon credit issued to the methodology more broadly and the specific project.

Westpac also supports Government steps to ensure process simplicity and streamlining for determining additionality to avoid unpredictable or inconsistent outcomes to project assessment.

Westpac supports recent amendments to the legislation to address concerns over the previous policy indications that “Some projects may cease to be additional during their lifetime, for example because the project activity may become common practice.” However, we also note that the definition of ‘common practice’ has not been prescribed in the legislation. Westpac would support greater clarity around defining ‘common practice’ and the factors involved in making this assessment, as this will allow investors to judge whether a particular practice is likely to remain ‘additional’ for a sufficient period of time to ensure revenue return.

Where an investment is made to generate a revenue stream from credits issued over a prescribed period of time, changing the revenue streams of the project in this manner and over the proscribed crediting period may adversely impact the ability to secure finance. Financiers, both equity and debt, would be reluctant to support projects if there is risk of revenue from credit generation ceasing or significantly reducing during the minimum return period for the capital invested.

In circumstances where the Government does feel it is appropriate to re-evaluate the additionality of approved methodologies, the Government should strongly signal well in advance that credits will no longer be eligible from a particular methodology and extreme care should be taken to ensure that existing projects are not adversely impacted financially in the immediate term. This will help to address ongoing concerns over the impact of short term regulatory changes to the commercial viability of the carbon farming market.

Creating Kyoto-compliant credits

Westpac notes that Kyoto-compliant carbon credits will only be issued for abatement achieved in the period 2008-2012 (the Kyoto abatement deadline). Given the proposed timeframe for implementation of the Carbon Farming Initiative, this would allow for a very limited period of time in which new projects can be established and achieve significant abatement eligible for the crediting of Kyoto-Kyoto compliant carbon credits.

Westpac recognizes that international uncertainty around the post-2012 market will make it difficult for the Government to clarify the post-2012 credit issuance regime in the immediate term, but would strongly encourage the government to make the appropriate arrangements necessary to clarify the continued export of Kyoto-compliant CFI credits for the post-2012 period as soon as is possible. Failure to do so would undermine the early growth of the domestic carbon offset market by



Submission Institutional Bank

adversely impacting the commercial viability of many carbon farming projects where the return period for capital invested extends beyond 2012.

Crediting

Westpac would support using the Australian National Registry of Emissions Units for the purposes of issuing, transferring and cancelling ACCUs, both Kyoto compliant and non-Kyoto compliant credits.

Crediting periods

Westpac strongly supports the establishment of longer crediting periods, and in particular the decision to allow for seven, fifteen and twenty year crediting periods. The extension of crediting periods will have positive implications for cash flow certainty and opportunities for financing carbon farming projects

Consent

Westpac supports provisions to ensure that all parties with an 'eligible interest' are required to provide consent as part of the project approval process. In particular, Westpac strongly supports the proposal that documentary evidence be provided that the consent of all parties with a registered interest in the land be required prior to project approval.

Ensuring that a note is attached to the land title signaling the attachment of a carbon liability is also critical for financial institutions as scheme obligations would also need to be noted on mortgages along with a covenant outlining maintenance obligations (and corresponding costs).

Reporting

Westpac notes the reporting requirements attached to carbon farming projects. Westpac would support a requirement that all parties with an interest in the land title (and potentially subject to carbon liabilities) should also be notified of any relevant changes to the project, such as major natural disasters, via administrative reporting requirements.

Westpac notes the revisal of reporting projects at the project level to allow participants to chose between 1 or 5 year reporting and cease reporting upon maturity.

Westpac would note that more frequent reporting of project information would be preferable for the market as it provides greater transparency around the stream of credits being issued, with implications for market expectations around pricing.

Register of CFI projects

Westpac strongly support the establishment of a national registry of Carbon Farming Initiative projects.

Westpac would also support promoting maximum transparency around the attachment of carbon liabilities to land title by ensuring that mandatory information requirements include explicit cross-reference to land title and the attached carbon liability (maintenance provisions).

Westpac would support efforts to allow for further detail on the co-benefits attached to particular projects (social or environmental) to be made available on the project database as this will influence price outcomes.



4. Personal security implications

Westpac notes that the Bill does not appear to address the implications of the Personal Property Securities Act 2009 (PPSA) and subsequent security implications. According to Division 3, [^] 150 of the Carbon Credits (Carbon Farming Initiative) Bill 2011 an Australian carbon credit unit is designated 'personal property'.

Section 8 of the Personal Property Securities Act 2009 ("PPSA") does not include Australian Carbon Credit Units in the list of interests to which the PPSA does not apply. Accordingly we conclude that it is the intention that the PPSA will apply to Australian carbon credits. This raises the following issues for further consideration:

- Consideration will need to be given as to how lenders will take a security interest over an Australian carbon credit unit?
- It is unclear how the security interest of lenders over carbon rights will be recorded under the Personal Property Securities regime?
- It is unclear how any transfer or transmission of an Australian carbon credit unit, including under [^] 151 (Transfer of Australian carbon credit units) and [^]152 (Transmission of Australian carbon credit units by assignment) of the Bill, will be impacted by, and will impact Personal Property Securities provisions pertaining to transfer and assignments of personal property?

Westpac notes that within New Zealand, amendments to the Personal Property Securities Act 1999 (PPSA) in September 2008, mean that carbon credit units (New Zealand Units or NZUs) are now within the definition of 'investment securities' for the purposes of the PPSA. Westpac New Zealand is therefore able to take security over NZUs by registering a security interest on the PPSR similar to the manner in which it would take security over company shares.

Given the above, Westpac notes that provisions will need to be made as to how the existence of a security interest over Australian carbon credit units will impact upon and need to be taken into consideration in relation to more standard security interests taken to support lending facilities.

5. Australian National Registry of Emissions Units Bill 2011

Westpac supports the formalization of the Australian National Registry of Emissions Units (ANREU) and the inclusion of CFI credits within this electronic registry.

The establishment of a single, electronic registry which tracks all ACCUs within Australia (both compliance and voluntary credits) will facilitate greater transparency at both the company and project level, thereby promoting greater price transparency within the Australian market.

Westpac also supports efforts to allow for further detail on the co-benefits attached to particular projects (social or environmental) to be made available on the project database.

6. Carbon Credits (Consequential Amendments) Bill 2011

Westpac notes the provisions detailed in the Carbon Credits (Consequential Amendments) Bill 2011, particularly as they relate to obligations for financial institutions under:

- Regulating the buying and selling of these units on behalf of another person as a 'designated service' under the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006*.
- Defining ACCUs and eligible international emissions units as financial products within the application of provisions relating to financial services and markets, and product disclosure, under Chapter 7 of the *Corporations Act 2001*.