

# Safeguard Mechanism (Crediting) Amendment Bill 2022

Submission to the inquiry by the Environment and  
Communications Legislation Committee

January 2023



60 Leicester Street,  
Carlton Vic. 3053

[admin@dea.org.au](mailto:admin@dea.org.au)  
[www.dea.org.au](http://www.dea.org.au)

DEA Scientific Committee:

Prof Colin Butler  
Prof David de Kretser AC  
Prof Robyn McDermott  
Prof Emeritus Sir Gustav Nossal AC  
Prof Fiona Stanley AC

Prof Stephen Boyden AM  
Prof Peter Doherty AC  
Prof Stephen Leeder AO  
Prof Lidia Morawska  
Prof Hugh Possingham  
Dr Rosemary Stanton OAM

Prof Emeritus Chris Burrell AO  
Prof Michael Kidd AM  
Prof Ian Lowe AO  
Prof Peter Newman AO  
Prof Lawrie Powell AC  
Dr Norman Swan

Doctors for the Environment Australia (DEA) is an independent, self-funded, non-government organisation of medical doctors and students in all Australian states and territories.

DEA's work is based on the premise that humans need a future with clean air and water, healthy soils capable of producing nutritious food, a stable climate, and a complex, diverse and interconnected humanity whose needs are met in a sustainable way. We are therefore interested in environmental protection and restoration to promote human health and social stability.

DEA's work is supported by a distinguished Advisory Committee of scientific experts whose knowledge of medical and public health issues is fully contemporary. Our members work across all specialties in community, hospital, and private practices.

DEA welcomes the opportunity to provide a submission to the Australian Senate on the health aspects of a revision of the Safeguard Mechanism at a time when human health and the environment are facing massive challenges due to unrestrained release of greenhouse gases.

Australia's commitment to a 2030 target of reducing emissions by 43% is not adequate to prevent global heating of 1.5degrees but is a step in the right direction. Even that modest target will not be reached if the Safeguard Mechanism has a flawed design. Recent extreme flood events in Pakistan, Lismore and the Kimberley illustrate that while temperature rise is progressing as predicted by climate models, extreme weather events have become more frequent and more extreme than predicted by most modelling. The problem is increasingly urgent, Australians have voted for climate action, we do not have another decade to waste.

## DEA position on the mechanism design: how SMCs are created and issued

- We support the implementation of the Safeguard Mechanism, a cap and trade system, if it is rigorously designed to reach Australia's carbon emission objectives.
- Two key features of a properly designed scheme are firstly that the cap is rigid and cannot be expanded to include new industries or increased output, and secondly it must lead to real reductions in emissions by being not overly reliant on offsets.
- A scheme that does not meet these requirements should be rejected by the senate.

## Glossary

**Headroom:** When a facility has its cap set at more than it currently emits. The Australian Conservation Foundation has found companies that have been given baselines double their current emissions, and in one instance 20 times higher. Headroom must be removed, or it will create a cash bonanza in SMC sales.

**SMC:** Safeguard Mechanism Credit. A certificate issued to a facility that emits less than its allowed cap. The credit is similar to an ACCU, and can be kept for future years or sold to another facility.

**Gross Emissions:** the amount of CO<sub>2</sub> equivalent gases that a facility releases, as opposed to Net Emissions which is the remainder after deducting any ACCUs or SMCs the facility may have bought.

**ACCU:** Australian Carbon Credit Unit. These mostly come from land use change projects, and many of them have been found to be invalid. A company required to offset emissions can purchase ACCU certificates and surrender them to the government, at which time they cease to exist. However, the land use change that gave rise to the certificate is required to persist in perpetuity.

**CO<sub>2</sub>e:** Carbon dioxide equivalent emissions. This is the sum of the CO<sub>2</sub> plus other gases multiplied by a factor for how damaging they are in climate terms. Methane is multiplied by 25 and is the most important other greenhouse gas.

**Emissions intensity:** A method of setting caps for individual facilities that takes account of production levels. The cap will be tonnes CO<sub>2</sub>e per unit of production. The alternative option of absolute caps sets a value in tonnes CO<sub>2</sub>e per year. The two methods can sensibly be combined by using whichever is lower.

**Carbon leakage:** The process by which production is shifted to jurisdictions with no carbon price or emission controls. Imports from cheap and dirty countries can compete with local low emissions production which has higher costs. Europe has imposed a Carbon Border Adjustment Mechanism starting in January 2023 to counteract carbon leakage, and other jurisdictions will probably follow.

**Cap and Trade:** An emissions reduction mechanism in which a cap is set for total economy wide emissions. Individual polluters are given permits to pollute, and if they can reduce their emissions to less than the permits they hold, residual permits can be sold to other companies. The cap is progressively reduced over time.

## Overall design

The safeguard mechanism is a grandfathering system to allow existing high emissions industries to continue to pollute for free, as long as they reduce emissions in line with an annual decrease of 4.9%.

Setting the emissions caps and removing headroom will be a difficult technical process that must be settled by regulators on one side and industry on the other. There is considerable scope for economic advantage to be gained by industrial operators exerting undue influence on regulators through political and legal pressure or other ways of gaming the system. The history of the Safeguard Mechanism to date has been complete failure due to weak intent and regulatory capture. A carbon tax is a much simpler solution that provides incentive to reduce emissions and is inherently fair both within and between countries. It would also raise revenue to be used on essential government services and protect Australian exports from carbon border protection tariffs. Unlike a grandfathering scheme, a carbon tax does not selectively disadvantage new entrants.

## The problem of new entrants

If a new high emissions industrial operation is proposed, it will require an emissions allowance under the Safeguard Mechanism. Granting new entrant operators a new cap will increase national emissions and subvert the intent of the scheme. For the overall national emissions to follow the required trajectory to reach climate objectives new entrants must be required to find emissions permits from within the existing total cap. This is possible through the trading of SMC certificates. Existing operations that have decreased their emissions by more than required can sell their excess permits. New entrants can avoid this cost by designing their industrial process to have zero emissions. It may well have the effect of making new coal and gas projects economically unviable, and this is a good outcome in the national interest.

If new entrants are granted emissions budgets outside the original Safeguard Mechanism total, it is essentially a cap and trade system without a cap, and would be worse than useless. It would not meet Australia's objectives and it should be rejected by the Senate.

The design of the Safeguard Mechanism specifically favours existing industrial facilities at the expense of new entrants. The proponent of a new industry such as a lower (but not zero) carbon steel works will be at

an economic disadvantage relative to existing competitors who are granted pollution rights for free. This is a perverse outcome that would not occur with a uniform carbon tax and will need to be addressed by other aspects of industry policy.

## Use of offsetting

Allowing emissions within the Safeguard scheme to be offset by ACCU or other certificates from outside the scheme puts the objective of emissions reductions at risk. Many of the activities awarded ACCU certificates have been found to be invalid on the grounds that they did not actually occur, would have occurred anyway, or are not permanent. The recent Chubb review has not fully addressed these concerns. If we cannot be certain of offsets created in Australia, there are even less grounds for confidence in offsets from overseas. Once the validity of Australian ACCU is re-established, they should be allowed to be used only in a limited capacity – for instance, to offset an aggregate maximum of 1 year’s change.

## Trade exposed industries

While it is tempting to avoid ‘carbon leakage’ by exempting exporting industries (or industries that face competition from imports) from extra costs of the Safeguard Mechanism, such exemptions would undermine the scheme. It would effectively be saying to the world that Australia will do nothing on emissions until all other countries take action. Special measures for trade exposed industries will lead to intense jockeying for favourable treatment and outcomes that nobody is happy with. Over time, it could lead to corrupt conduct.

## Coverage

The scheme coverage of facilities emitting 100,000 tonnes per year should be a one-way street, that is, facilities do not leave the scheme when emissions drop below the threshold. The threshold for new entrants should be lower to avoid gaming. Under current proposals, two adjoining projects each of 90,000 tonnes annual emissions would not be covered by the scheme, so the new entrant threshold should be 25,000 tonnes, and the scheme threshold should decrease each five years to increase coverage across the economy.

## An Example

A coal mine has fugitive methane emissions as well as CO<sub>2</sub> emissions from its operating machinery. If the current emissions are 200,000 tonnes CO<sub>2</sub>e per year it would be given a cap of 200,000 for 2023 and 190,200 for 2024, and so on. If the mine has a remaining life of 5 years it would be granted a decreasing cap for 5 years only. This leads to several conundrums:

- If the caps are set on an “emissions intensity” basis, the 2024 cap would not be an absolute number but a value for CO<sub>2</sub>e per tonne of coal produced. The mine would not have the option to reduce emissions by reducing coal output, as the cap would decrease in proportion. It would have to implement other measures such as replacing mine machinery with zero emission variants or changing mining methods to reduce or capture fugitive methane. Likewise, if the operators choose to, they could increase production and be automatically granted permission to emit more CO<sub>2</sub>e. As yet, there is no proposal to stop this from increasing the total of national emissions and subverting the intent of the scheme.
- If economics change and the mine decides to close after 4 years instead of 5, what happens to its cap? If the cap is set on an absolute basis the owners would be able to sell their CO<sub>2</sub>e allowance to another company. This is in effect a public payment to a polluting industry to stop polluting. This

approach has been adopted in various countries but does not seem to be a good use of public money. If the cap is set on an emissions intensity basis zero production would give a zero cap, avoiding this situation. A closed mine will continue to leak methane in subsequent years until effective rehabilitation has been completed. The Safeguard Mechanism must be designed to impose a cost on companies that allow ongoing fugitive emissions.