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25 January 2023

Committee Secretary  
Senate Standing Committees on Environment and Communications  
PO Box 6100  
Parliament House  
Canberra ACT 2600

*Submitted via Committee website*

Dear Committee Members,

**RE: Orica's Submission to the Committee's inquiry into the *Safeguard Mechanism (Crediting) Amendment Bill 2022***

Thank you for the opportunity to contribute to the Committee's examination of the *Safeguard Mechanism (Crediting) Amendment Bill 2022*.

At the outset, we should acknowledge a point that the Committee is likely aware of; that this Bill is part of a suite of Bills and disallowable instruments which are expected to be considered by the Parliament in March 2023 and which seek to reform the operation of the Safeguard Mechanism which is slated to commence in its revised form from 1 July 2023.

Much of this broader package has only been clarified and made public inside these last two weeks and we are still assessing the detail and potential impact on Orica's past and planned investments in decarbonisation. As such, we wish to make clear that the views we have expressed in the submission accompanying this letter, represent our *initial* thinking which is likely to evolve during the course of the Committee's inquiry, including at the scheduled hearings, which we would welcome the opportunity to participate in.

Orica supports the Government's increased national commitments for emissions reductions and agrees that reform of the Safeguard Mechanism is required to deliver these commitments across Australia's heaviest emitters. Orica owns and operates two Safeguard Mechanism (SGM) liable facilities; our Newcastle and Gladstone ammonium nitrate manufacturing sites which collectively account for almost two per cent of total emissions from across the 215 SGM facilities. Our core products, ammonium nitrate and ammonia, are emissions-intensive, trade exposed and are critical inputs for the explosives and blasting systems we supply to Australian and overseas mines.

Orica is one of only a few companies within the chemical industry in Australia captured by the Safeguard Mechanism – a sub-sector of the broader industrial sector. Based on the latest forecasts, emissions from this sector are expected to remain steady between 2024 and 2035<sup>1</sup>. As such, revisions to the SGM scheme are required to drive improved levels of decarbonisation.

As you may be aware, Orica moved early, setting ambitious voluntary emission reduction targets and investing early in capital-intensive abatement projects. This includes deploying tertiary catalyst abatement technology to Australia for the first time at our Newcastle nitric acid plants on Kooragang Island; collaborations at both Gladstone and Newcastle to foster the growth of domestic green hydrogen hubs; and our long-standing investment in Mineral Carbonation International as we host their first Carbon Capture and Utilisation demonstration plant at Kooragang Island. Orica is also supporting Future Facing Industries such as eMobility through our partnership at Gladstone with AlphaHPA (High Purity Alumina), supplying two key process reagents (Ammonia & Nitric Acid) and being the offtake recipient for Alpha's by-product (Ammonium Nitrate); realising the potential of a circular economy for the industrial sector.

Orica led the chemical industry in Australia in setting corporate emissions reduction targets; to reduce operational scope 1 and scope 2 emissions by at least 40% compared to 2019 levels. As of end FY2022 our Scope 1 and 2 net emissions totalled 1,883 ktCO<sub>2</sub>-e, which represents a 14% reduction compared to 2019 levels. In 2022, Orica also set target to source 100% renewable electricity by 2040 with an interim step of 60% by 2030.

Reforms to the Safeguard Mechanism come at a time when Orica is part way through significant capital projects aimed to deliver on these emission reduction commitments, including consideration of investing in capital-intensive tertiary abatement technology for our nitric acid plants at our Gladstone ammonium nitrate manufacturing facility.

While supportive of the thrust of the government's *Safeguard Mechanism (Crediting) Amendment Bill 2022* and the *Safeguard Amendment Rules*, Orica is concerned with the erosion of the existing 'deemed surrender' provision and the investment uncertainty that will be created by changes, which apply retrospectively. Deemed surrender enables an entity with an approved ERF project and a Carbon Abatement Contract to sell ACCUs to the Commonwealth and retain the ability to count the associated emissions reductions towards the achievement of meeting the Safeguard Mechanism baseline (and any voluntary corporate targets). This benefit (which does *not* constitute a double-counting of emissions reductions) was deliberately designed to incentivise and help bring forward capital intensive investment in decarbonisation. It should be noted that these arrangements, while incentivising investment by companies, also enable the Commonwealth to purchase ACCUs at the *lowest cost*. Companies that execute these contracts with the Commonwealth are forgoing much higher prices for their ACCUs on the secondary market, in exchange for being able to retain the right to use the emissions reductions.

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<sup>1</sup> "[Australia's Emissions Projections 2022](#)" Department of Climate Change, Energy, the Environment and Water. December 2022. Refer to page 51.

The government in its latest consultation on SGM reform (released 10 January 2023) has stated an intention to retrospectively grandfather deemed surrender for two years, and then remove it altogether. Orica's contracts for the sale of ACCUs, entered in good faith, are for seven years. It is likely there are only a handful of entities with direct experience with this particular feature of the Scheme and who now find themselves facing retrospective changes. As such, our views on the value of deemed surrender for existing ERF projects, as an instrument for incentivising investment in decarbonisation particularly in the hard-to-abate industrial sector, are important for the Committee to appreciate with the goal of avoiding unintended policy consequences and perverse outcomes for the environment.

We look forward to elaborating on our experiences and to aiding the Committee's understanding of decarbonising our operations whilst competing in a globally competitive industry. Please direct all correspondence and inquiries to Mel Cheesman, Head of Government and Regulation [REDACTED]. Mel is also our contact point for arrangements for appearing before the Committee – an opportunity we would welcome.

Yours sincerely,

[REDACTED]

**Paul Evans**

Global Vice President Corporate Affairs

Enclosed:

1. Orica's submission –three pages.
2. Attachment A: Understanding Orica's use of deemed surrender – two pages.
3. Attachment B: Understanding the double-benefit that deemed surrender provides – one page.

## ABOUT ORICA

Orica, headquartered in Australia and ASX100 listed, is one of the world's leading mining and infrastructure solutions providers, operating in 100 markets. From the production and supply of explosives, blasting systems, mining chemicals and geotechnical monitoring, to our cutting-edge digital solutions and comprehensive range of services, we sustainably mobilise the earth's resources.

Orica is committed to achieving net zero emissions by 2050, with an interim operational emissions reduction target of at least 40% by 2030 based on 2019 levels. At the end of the 2022 reporting period, global scope 1 and 2 emissions were 14% below our 2019 baseline. In 2022, Orica set a renewable electricity target committing to sourcing 100% renewable electricity by 2040, with an interim step of 60% by 2030. As of FY22, 84% of Orica's global operational scope 1 emissions were subject to direct emissions regulation.

## ORICA AND THE SAFEGUARD MECHANISM

Orica has two facilities captured under the Safeguard Mechanism (SGM); Orica Yarwun near Gladstone in Queensland, which produces ammonium nitrate and Orica Kooragang Island (KI) near Newcastle in New South Wales, which produces both ammonium nitrate and ammonia. These products are vital for the continuity of operations across the domestic mining sector and are globally in short supply, owing to the almost universal trade sanctions currently in place on goods manufactured in Russia and Russia's standing as one of the largest global producers of ammonium nitrate. Both of Orica's facilities have registered projects under the Emissions Reduction Fund (ERF), which gives Orica the ability to generate Australian Carbon Credit Units (ACCUs). Both facilities produce Emissions Intensive, Trade Exposed (EITE) goods. Orica entered Carbon Abatement Contracts with the Commonwealth, for both ERF Projects and these contracts were instrumental to investment case consideration in a global market.

To date, Orica's approach to decarbonisation has been centred on tackling those areas within our control. We operate nine Nitric Acid plants globally, with nitrous oxide (N<sub>2</sub>O) emissions representing 49% of our total scope 1 and 2 operational emissions (as tCO<sub>2</sub>-e). Since 2018, we have undertaken a range of operational N<sub>2</sub>O abatement trials and continued to focus our decarbonisation studies on these continuous manufacturing facilities where we are targeting substantial reduction in nitrous oxide emissions.

Relevant to our Australian operations, since 2021/2022 we have:

- Continued our nitrous oxide abatement catalyst trials at Kooragang Island (NSW) where we have three Nitric Acid Plants (NAPs);
- Sanctioned the Kooragang Island Decarbonisation Project with project partners: the NSW Government, Clean Energy Finance Corporation, Australian Government, and ThyssenKrupp. The project is registered through the Emissions Reduction Fund (ERF), with a secured Carbon Abatement Contract to potentially deliver ~3.37 million tonnes of abatement through the installation of best available abatement technology on all three Nitric Acid plants from October 2022;
- Registered the Yarwun Nitrates Decarbonisation Project (QLD) in March 2022 for our three Nitric Acid Plants (NAPs), and subsequently secured a carbon abatement contract through the ERF, to potentially deliver 1.3 million tonnes of abatement.

In conjunction with registering an Emissions Reduction Fund (ERF) Project and securing a Carbon Abatement Contract (CAC) with deemed surrender, the partial funding from the NSW State Government and debt-finance from the Clean Energy Finance Corporation were

fundamental in building a delivery model and securing internal funding for the \$37m Kooragang Island Decarbonisation Project.

Similarly, successful registration of an Emissions Reduction Fund (ERF) project and a secured Carbon Abatement Project have underpinned our feasibility study and business case for the Yarwun Decarbonisation Project. Without this support being confirmed, and grandfathering of existing provisions (e.g., deemed surrender), the Yarwun Decarbonisation Project is at risk of being deferred to much later in the decade. In August 2022, Orica's Global Investment Committee deferred a final investment decision on the project on account of uncertainty presented by the proposed SGM reforms.

Orica is presently considering the detail of the final release of SGM Scheme reform proposals from the Government, published 10 January 2023. The importance of the deemed surrender provision, compared with the untested benefits afforded by newly revealed details for Safeguard Mechanism Credits is still being assessed.

At the time of writing, we can however confirm the following:

1. Orica supports the Government's broader climate change priorities, including lifting Australia's national emissions reduction goal to 43 per cent by 2030 and a more robust Safeguard Mechanism (SGM) to drive decarbonisation of the industrial sector.
2. Orica welcomes the removal of headroom and the proposed decline in baselines as a means to accelerating decarbonisation.
3. Orica welcomes the proposed hybrid approach to setting baselines – to be addressed via amendment to the *National Greenhouse and Energy Reporting (Safeguard Mechanism) Amendment (Reforms) Rules 2023 (The Safeguard Rules)*.
4. Orica welcomes the creation of Safeguard Mechanism Credits and is currently assessing the detailed information released 10 January 2023, to understand how they compare with ACCUs and deemed surrender.
5. Orica welcomes tailored support for EITEs and the development of a dedicated 'Safeguard Transformation Scheme' under the 'Powering the Regions' Fund.

To aid the Committee's understanding of deemed surrender, we submit two attachments, which we hope will further understanding of this Scheme element and of why it has been of particular value to Orica in providing confidence for moving early to invest in expensive decarbonisation technology and for underpinning the making of our corporate commitments to reduce emissions (40% on 2019 levels by 2030 and net zero by 2050).

The second of these attachments (Attachment B) explains that deemed surrender does not result in double-counting of emissions reductions, but it does importantly provide a 'double benefit'. Orica notes that during the course of the debate on SGM reform, 'double-counting' and 'double-benefit' may have been conflated. This has been to the detriment of an accurate understanding of deemed surrender – an important and legitimate aspect of the ERF scheme that has incentivised early investment in decarbonisation. Any amendment to this provision should not penalise early-movers who utilised this provision in good faith, to secure the business case for investment in decarbonisation.

In considering how the Government intends to use the *Safeguard Mechanism (Crediting) Amendment Bill 2022*, together with proposed amendments to *The Safeguard Rules* (which has just recently been released as an Exposure Draft) to retrospectively make changes to deemed surrender, it is worth considering that the current proposal differs markedly from what

was released for public consultation in August of 2022, being:

1. "Removing deemed surrender provisions for existing ERF contracts held by Safeguard facilities, and facilities that become covered by the Safeguard Mechanism, and establishing no new deemed surrender arrangements; or
2. Continuing existing deemed surrender arrangements for facilities with an ERF contract, for the duration of their existing contract (a grandfathering approach). Deemed surrender would not be available under any new ERF contracts entered into after the release of this consultation paper. The approach would be implemented through primary Act and subordinate legislative changes."<sup>2</sup>

The new proposal, released 10 January 2023, is for deemed surrender to only be grandfathered for two years and then removed altogether. The terms of Carbon Abatement Contracts are seven years. The possibility of retrospectively limiting deemed surrender, if applied, will send a concerning message to would-be investors in Australia.

We look forward to the Committee's hearings and to the opportunity of elaborating and clarifying Orica's views on the legislative package.

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<sup>2</sup> "Safeguard Mechanism Reforms" Commonwealth Department of Climate Change, Energy, the Environment and Water, Refer to pages 18 and 19.

## ATTACHMENT A – UNDERSTANDING ORICA’S USE OF DEEMED SURRENDER

**Deemed surrender enables an entity to surrender ACCUs to government to achieve an emissions reduction AND to also receive payment under an ERF Carbon Abatement Contract**

You need **‘two passes to play’** to be able to **utilise** the **‘deemed surrender’** provision: **1)** have successfully registered an **Emissions Reduction Fund (ERF) Project**; this **qualifies your abatement** activity as being additional (above business-as usual) **to be able to generate Australian Carbon Credit Units<sup>3</sup> (ACCUs)**, and **2)** to have bid at auction to secure and execute a **Carbon Abatement Contract (CAC)**; a **contract with the Commonwealth** where an entity agrees to supply government with an agreed number of ACCUs, within an agreed timeframe, for a set, confidential price. Orica’s two CACs are ‘optional delivery contracts’, meaning Orica has secured the right, but not the obligation, to sell carbon abatement to the Commonwealth.

**Deemed surrender is important to Orica because it allows us to do two things:**

1. **Meet our voluntary corporate emissions reduction commitments**, which we led the chemical industry in setting, including our target to reduce Scope 1&2 emissions by at least 40% by 2030 (on FY2019 levels) and our ambition to achieve net zero by 2050; **and**
2. **Monetise our ACCUs** to help us recover some of the significant capital investment deployed to secure best-in-class abatement technology for our nitric acid plants (the first such technology deployment in Australia.)

**Q:** But **wouldn’t Orica earn more for its ACCUs if they were sold on the secondary market**, rather than under contract to government? Orica’s ‘optional delivery contract’ terms would allow for this flexibility, right?

**A:** **Yes – but** if you sell your ACCUs on the secondary market **you can’t then also claim the emissions reduction** and we need that **for meeting our voluntary corporate targets**.

**The ‘Safeguard Mechanism (Crediting) Amendment Bill 2022’, together with the ‘National Greenhouse and Energy Reporting (Safeguard Mechanism) Amendment (Reforms) Rules 2023 (The Safeguard Rules)’, seek to fundamentally alter deemed surrender, retrospectively.**

- In the first SGM Consultation Paper released 18 August 2022, two possible options were presented for the future treatment of deemed surrender. Option 1 was for the retrospective removal of deemed surrender and Option 2, which Orica supported, read as follows: *“Continuing existing deemed surrender arrangements for facilities with an ERF contract for the duration of their existing contract. Deemed surrender would not be available under any new ERF contracts entered into after the release of this consultation paper.”*

<sup>3</sup> Each ACCU represents one tonne of carbon dioxide equivalent (tCO<sub>2</sub>-e) emissions stored or avoided by an ERF project. ACCUs can be sold to generate income – either to government (under contract) or on the secondary market.



- On 10 January 2023, the Government released a Position Paper, detailing the proposed revisions to the operation of the Scheme. **On the treatment of deemed surrender, the proposal does not reflect either of the two options presented in the August 2022 consultation paper**, but instead proposes this:

*“Existing contracts for Government purchase of ACCUs will remain in place, and ‘deemed surrender’ provisions would be grandfathered for two years. This means facilities with existing contracts can continue to sell their ACCUs to the Government for the contract duration, but could only count the associated abatement towards their baseline for the first two years.”*

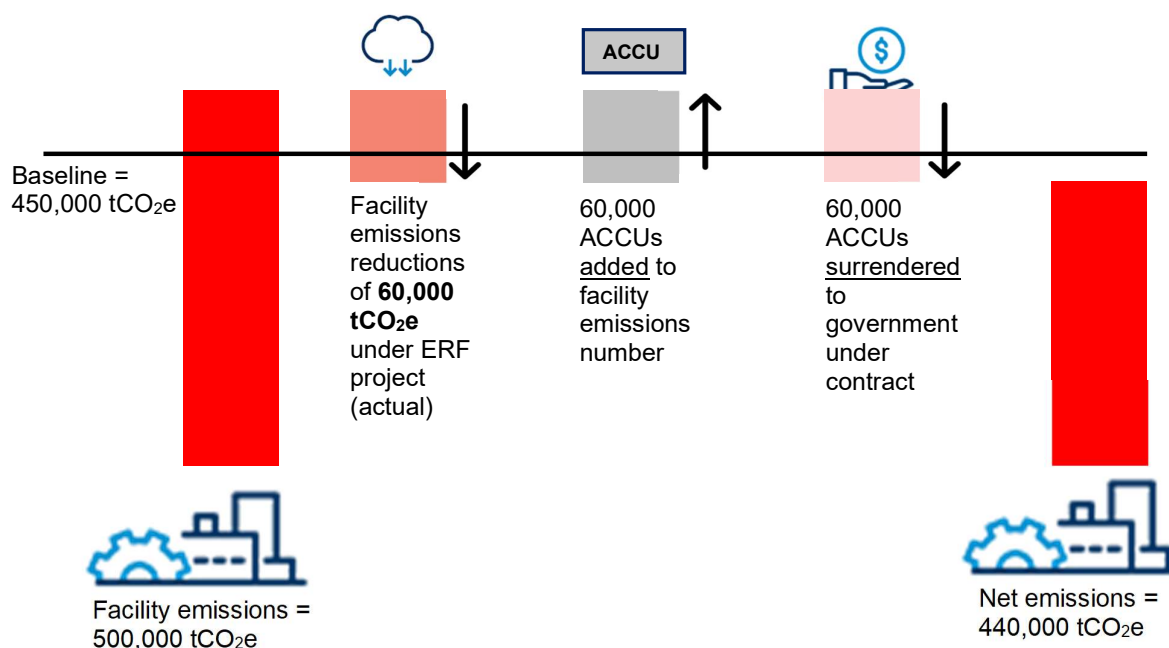
- Carbon Abatement Contracts span seven years – and Orica entered these in good faith and expected to be able to count the associated abatement towards our baseline for the duration of the contracts. The latest proposal removes this option, retrospectively.
- The *Safeguard Mechanism (Crediting) Amendment Bill 2022* seeks to amend section 22XN of the NGER Act to make it possible for deemed surrender to be revised retrospectively – *the exact revision being then enacted* via subsequent amendment to the *National Greenhouse and Energy Reporting (Safeguard Mechanism) Rule 2015*.
- As such, grandfathering of deemed surrender provisions for two years, is intended to be provided for, as follows:
  - Through the *Safeguard Mechanism (Crediting) Amendment Bill 2022* at Item 33 of Schedule 1, which creates a new subsection 22XN97, together with;
  - Items 53 of Schedule 1 (new sections 72C) of the *National Greenhouse and Energy Reporting (Safeguard Mechanism) Amendment (Reforms) Rules 2023* (for which an Exposure Draft was released 10 January 2023 and intended for tabling in March 2023, following consultation).



## ATTACHMENT B – UNDERSTANDING THE ‘DOUBLE-BENEFIT’ DEEMED SURRENDER PROVIDES

**Deemed surrender does not constitute double-counting of emissions and the NGER Act prevents this from occurring.**

Safeguard Mechanism (SGM) entities are required to reduce their emissions to ensure they remain below their SGM baseline. The *National Greenhouse and Energy Reporting (NGER) Act 2007*, as amended by the *Carbon Farming Initiative Amendment Act 2014*, ensures that emissions reductions are not counted more than once, by adding ACCUs issued for emissions reductions at a facility, back onto that facility's net emissions. In practice, this works as follows:



In this fictitious scenario, **Orica has emissions of 500,000 tCO<sub>2</sub>e** and as a Safeguard Facility, its **baseline has been set at 450,000 tCO<sub>2</sub>e**. Orica **reduces emissions by 60,000 tCO<sub>2</sub>e, generating 60,000 ACCUs**. (Each ACCU represents one tonne of carbon dioxide equivalent stored or avoided by an ERF project.) **The ACCUs are added to Orica's emissions profile** and are **only deducted when Orica surrenders these 60,000 ACCUs to the Government under its Carbon Abatement Contract**.

Deemed surrender means Orica is paid for the ACCUs surrendered to government AND can claim the achievement of an emissions reduction of 60,000 tCO<sub>2</sub>e towards its own corporate emissions reduction targets and safeguard compliance obligations. In this way, **deemed surrender does provide a 'double benefit' but does not constitute 'double-counting' of emissions reductions**. **'Double-benefit' and 'double-counting' have become conflated in the SGM reform debate and created confusion**. Receiving ACCUs and Safeguard Mechanism Credits (SMCs) for the same tonne of CO<sub>2</sub> reduced *would* amount to double-counting and Orica opposes this. In fact, Orica argues that a facility should not be able to generate ACCUs and SMCs in the same financial year. Its one, or the other – not both.

Deemed surrender enables Orica to claim the benefit of emissions reductions achieved with government support (with government purchasing the ACCUs under contract at lowest cost) and in this way enables the same benefit realised by other entities who receive government funding (ARENA or similar) to achieve emissions reductions.