

# **AIGN Comments on Carbon Credits (Carbon Farming Initiative) Amendment Bill 2014**

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## 1 BACKGROUND

AIGN welcomes the opportunity to provide comments on the draft legislation to give effect to the implementation of the Emissions Reduction Fund (ERF) crediting and purchasing arrangements. However, the time available between the release of the draft legislation and the due date for submissions was very short (even more so considering other consultation processes occurring within this time). This presents difficulties for stakeholders to provide considered and useful feedback.

In reading this response, the Department should note AIGN's broad range of members, and resultant wide diversity of views on greenhouse and energy policy. This submission accords with the views of our members in general. However, at times, there are variations in the positions of individual members on specific issues. It is therefore important that the Department considers AIGN's feedback alongside any responses made to the draft legislation by our members.

## 2 INTRODUCTION

AIGN supports the three principles that have guided decisions on the design of the ERF, namely lowest cost emissions reductions, genuine emissions reductions, and streamlined administration. They are consistent with AIGN principles advocating policy approaches based, as far as is practicable, on market mechanisms with the objective of least cost abatement (both domestic and international), underpinned by streamlined, transparent, efficient and effective administrative, reporting and compliance arrangements. In addition, AIGN proposes a fourth principle: ensuring competitiveness. Our climate policy framework must maintain the competitiveness of entities operating in Australia, to avoid leakage and thereby ensure that emissions reductions result in a genuine lowering of global emissions.

Accompanying these principles is the need for long-term policy stability to encourage industry investment. In our submission to the ERF Green Paper, AIGN proposed that the stability of the ERF be enhanced by building in flexibility in terms of contract periods. Providing policy stability will prevent risks such as short-term, restricted applications and limited participation (potentially cutting out genuine low-cost abatement options), and it will also support the nature of commercial arrangements such as forward delivery contracts. AIGN observes with disappointment that these provisions remain, for the most part, unchanged since the Green Paper was released.

AIGN notes that the ERF's "overriding objective...should be to purchase emissions reductions at the lowest available cost".<sup>1</sup> Consistent with the AIGN principle of least cost abatement, the ERF should provide access to international units. This will promote genuine emissions reductions, assist with maintaining Australia's competitiveness, and address the potential for leakage.

## 3 SAFEGUARDING EMISSIONS REDUCTIONS

Although aware that the draft legislation focuses on crediting and purchasing abatement, AIGN wishes to emphasise again the importance of consulting extensively on the safeguarding arrangements. While the proposed implementation timeframe provides the opportunity for considered development of the mechanism, 1 July 2015 is an ambitious start date given the complexity of discussions required.

AIGN acknowledges the confirmation by the Government that the ERF will not be revenue raising, nor will it penalise businesses who continue to operate on a 'business as usual' basis.

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<sup>1</sup> Emissions Reduction Fund Green Paper, Commonwealth of Australia, 2013, p 18.

We note that a number of decisions on the design of the safeguarding mechanism were made in the ERF White Paper, chiefly in respect of coverage and setting emissions baselines. The safeguarding mechanism will cover facilities with direct emissions of 100,000 t CO<sub>2</sub>-e or more per annum, or about 52 per cent of Australia's emissions. AIGN accepts the administrative advantages of limiting coverage; at the same time, AIGN draws attention to the Government's intent for the mechanism to ensure emissions reductions paid for through the ERF are not displaced by significant rises elsewhere in the economy. The safeguarding mechanism will leave about 48 per cent of Australia's emissions uncovered, creating the possibility for economy-wide emissions to rise outside the scope of the mechanism. Entities covered under the safeguarding mechanism must not bear the burden of rises in uncovered emissions in any way.

Regarding the setting of emissions baselines, AIGN notes the White Paper decision to set baselines at the highest level of absolute emissions over the historical period 2009/10 to 2013/14, based on NGERS data. Consistent with the Government's policy of encouraging economic growth and not penalising 'business as usual' activity, AIGN promotes consultation with individual entities and/or industry sectors who may have special circumstances to discuss regarding baselines.

As highlighted in AIGN's ERF Green Paper submission, there should be a right of review for an entity if it exceeds its baseline, providing the opportunity to supply context for any temporary anomalies or to adjust the baseline. If entities exceed baselines, the safeguard arrangements should provide the opportunity for acquittal using domestic and international permits.

## 4 PURCHASING EMISSIONS REDUCTIONS

### 4.1 Purchase Contracts

AIGN is disappointed that some of our recommendations designed to improve policy stability have not been adopted, particularly in relation to the term of contracts. The ERF needs to provide industry with the certainty and stability required to encourage rational business decision-making. AIGN urges reconsideration to allow contract terms longer than 5 years. Commercial investment decisions relating to energy use are among many variables that a company will need to consider for any investment requiring capital. Therefore, the ERF needs to be long-term in nature to encourage genuine, low-cost abatement.

We welcome the opportunity for input to a consultant prior to the first auction to assist the Government in understanding the practicalities of devising a project proposal and the influence of the fixed contract term on this process. However, initial projects may well not be representative of projects in the longer term (e.g. proponents might be putting forward more moderate projects as a testing exercise). Therefore, the Government should maintain access to independent advice through a consultant as the ERF evolves. In this way, it is hoped that genuine (and possibly low-cost) abatement options will not be missed due to an arbitrary cut-off date and a lack of flexibility.

### 4.2 Methodologies

AIGN supports endeavours to streamline the development of methodologies by increasing the Minister's and the Emissions Reduction Assurance Committee's (ERAC) discretion and flexibility. It will be important to avoid the costs in time and resources associated with the current complex and lengthy CFI accreditation process.

Government officials have indicated that the ERAC will include the current Domestic Offsets Integrity Committee (DOIC) and be expanded by a further two members. The mix of membership must ensure that representatives with

industry expertise currently not required under the CFI are adequately present, to allow for the expansion in methodology type that will become eligible to apply to the ERAC.

### 4.3 Additionality

The amended additionality provisions requiring a project to be new, and unlikely to occur because of funding from another programme, are positive steps toward simplifying this element of registration. AIGN draws specific attention to paragraph 1.55 in the explanatory memorandum (p 18), which indicates a level of flexibility for determining whether emissions reductions meet these requirements. We believe this flexibility should encompass consideration of several additional factors. For example, an entity may have implemented a project that made economic sense within the context of the carbon price, but that will be discontinued when the carbon price is removed. While not meeting the technical definition of “new”, it should still be considered additional under the ERF because it would not be undertaken without a policy incentive. There may also be instances where an existing project can be improved, and increase its abatement, with support from the ERF; in such instances the additional abatement should be considered eligible to apply for funding.

### 4.4 Procurement

The explanatory memorandum explicitly consigns ‘significant discretion’ to the Clean Energy Regulator (CER) “...in the conduct of purchasing processes and [it] can purchase emissions reductions through other processes such as through a tender.” (paragraph 4.3, p 35) AIGN supports the potential for funds to be secured through tender as well as reverse auction; a tender will also allow market forces to determine the lowest cost abatement options through competition while being easily comprehended, administratively simple, transparent and scalable in operation.

However, details on how the auction process is proposed to operate remain scant, noting that the CER is to have a major role. Whilst appreciative of the independence and the expertise developed by the CER through administering NGERs and various other programs, an important principle of good policy is the separation of development from implementation. This separation is well established and should be maintained here also, for the benefit of administrators and participants. It is the expectation of industry that the Government will provide the CER with clear directions on the operation and management of the auction and tender (and any other procurement) processes. The CER should then establish the detailed implementation arrangements in close consultation with industry.

### 4.5 Price discovery

AIGN appreciates the perceived sensitivities around publishing the auction benchmark price, particularly in an environment where the number of bids may be limited. However, AIGN promotes the provision of aggregated information regarding auction results to enable some form of price discovery. While we recognise that the Government wishes to avoid a situation where bids may be inflated to the level of the benchmark price, the Government should also consider the implications of forcing entities to operate ‘blind’, with no way of ascertaining the approximate cost of abatement. In this environment, the rational decision for many entities will be to avoid the market altogether, and avoid the resource cost of developing proposals with no ability to evaluate their own potential competitiveness. Providing aggregated information after the conclusion of auctions would go some way to alleviate this problem. It would better enable entities to make informed judgements on whether to consider developing proposals, and assist to inform the market of the possible sources, magnitude and cost of future abatement.

## 4.6 Make-Good Provisions

AIGN notes that an entity that has signed a contract with the Government for providing abatement will be under a requirement to make good any shortfalls in delivery due to unforeseen circumstances. This is especially concerning because such entities will be reliant on a voluntary market whose future size and depth is, at present, unknown. This approach is clearly appealing to the Government as it transfers all of the risk onto ERF participants, but it will not act as an encouragement to potential project proponents.

AIGN recognises the need for abatement to be credible, and the need to rely on the ERF to deliver Australia's emissions reduction goals. The Government has alternative options to achieve these ends. One option is to enable entities needing to make good a shortfall to access the international market; this would alleviate industry concerns that participation in the ERF could inadvertently be a cost-negative exercise.

It must be acknowledged that another feasible scenario is the reverse: that an entity might pay less for international permits to make up their shortfall than they would have earned from delivering the contracted abatement. This would be avoided by adopting a variation of the above suggestion, in which the Government would pay the entity for the abatement delivered, withhold funding for the undelivered abatement, and go to either the domestic or the international market to make up the shortfall. Any remaining funding could be returned to the ERF for future auctions/tenders.

## 4.7 Auditing

AIGN supports a risk-based approach to auditing. Furthermore, there is a need to ensure greater commonality in determining the carrying out of audits (e.g. what information is to be provided to auditors). Currently there are variations between audits, sometimes dependent on service provider, which incur unnecessary costs on some entities. It is for instances such as this that AIGN has been advocating for the ability of the CER to issue ATO-style rulings to clarify regulations and assist in the seamless, efficient operation of the programs and schemes for which it has responsibility. The need is perhaps amplified by the relative newness and complexity of its portfolio of policy instruments. AIGN looks forward to further consultation with the CER on this matter.

# 5 OTHER ISSUES

## 5.1 Simplicity of Reporting (NGERS)

Companies who are not going to apply for funding under the ERF for emissions reduction opportunities, and are operating as usual, should not be burdened with any additional reporting requirements beyond those they already have under NGERS.

Recognising the ongoing important role NGERS is to play and in order to minimise the compliance burden on industry, the Government must examine approaches to streamlining NGERS, consistent with the requirement for detailed emissions information from industry. Whilst there have been a number of welcome changes to NGERS over the past year, more extensive reform is possible to improve the efficiency of reporting for companies through streamlining reporting obligations without affecting the quality of data collected.

The focus of NGERS into the future should be on reporting material emissions. The requirement for industry to estimate and report the uncertainty associated with emissions reported could be removed, and instead become a nationalised calculation undertaken by the Government, if needed under international reporting requirements. There are many other existing requirements on industry to report non-material emissions of a minor nature (but which are complex to report) that should be reviewed and removed if they no longer serve any useful purpose. Where

emissions are expected to fall below the threshold the reporter should be allowed to make estimations based on historical average.

The liability acquittal/payment process for Direct Action should also use existing CER account and liability transfer structures, where applicable, to limit administrative rework and enable entities with existing governance processes for the Carbon Pricing Mechanism to be retained for financial management purposes.

## 5.2 2015 Review

A review in 2015 should be implemented only if required; early reviews of new policies can encounter problems such as a lack of data and evidence on which to base a proper assessment. This review, if required, should be conducted by a credible independent agency that can bring the appropriate degree of objectivity to the subject.

## 5.3 Access to International Units

As previously highlighted and consistent with the AIGN principle of least-cost abatement through market mechanisms, AIGN supports the use of international units as an option to make up any failure to deliver the contracted amount of abatement, and as part of the safeguarding arrangements. This will assist Australia in meeting its international commitments, and endorses the comments of the Climate Change Authority that “the Government could consider using genuine international emissions reductions to complement domestic efforts to achieve Australia’s minimum 5 per cent commitment”.<sup>2</sup>

## 6 CONCLUSION

Thank you for the opportunity to provide comments on the draft legislation. AIGN looks forward to future engagement as the ERF is refined and implemented, and the safeguarding mechanism developed.

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<sup>2</sup> CCA Targets & Progress Draft Report, October 2013, p.13.