

26 September 2008

Committee Secretary
Senate Select Committee on Fuel and Energy
Department of the Senate
PO Box 6100
Parliament House
Canberra ACT 2600
Australia

Via email: fuelenergy.sen@aph.gov.au

Dear Secretary

Contractors and Carbon Trading

Leighton Holdings and its subsidiary companies have made a submission to the Carbon Pollution Reduction Scheme Green Paper. The submission outlines the Leighton Group's concerns and proposed changes to the Government's preferred emissions trading model.

The Leighton Group is Australia's largest mining and construction contractor, employing nearly 22,000 people domestically. Many of our employees work in rural and regional Australia.

Given the Committee's examination of the impact of higher petroleum, diesel and gas prices, I would like to draw your attention to the following impacts of the preferred CPRS model on the Leighton Group:

- Construction projects will be affected indirectly through rising input costs associated with a carbon price, increasing the cost of infrastructure.
- Mining projects, which employ more than 5,400 people, will be affected directly and drawn into the scheme even though our clients have more opportunity to reduce greenhouse gas emissions.
- Owner-operated landfill sites may be forced to close.

Please find attached a copy of our Green Paper submission.

Yours sincerely



Penny Bingham-Hall
Executive General Manager, Strategy

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SUBMISSION TO CARBON POLLUTION REDUCTION SCHEME - GREEN PAPER

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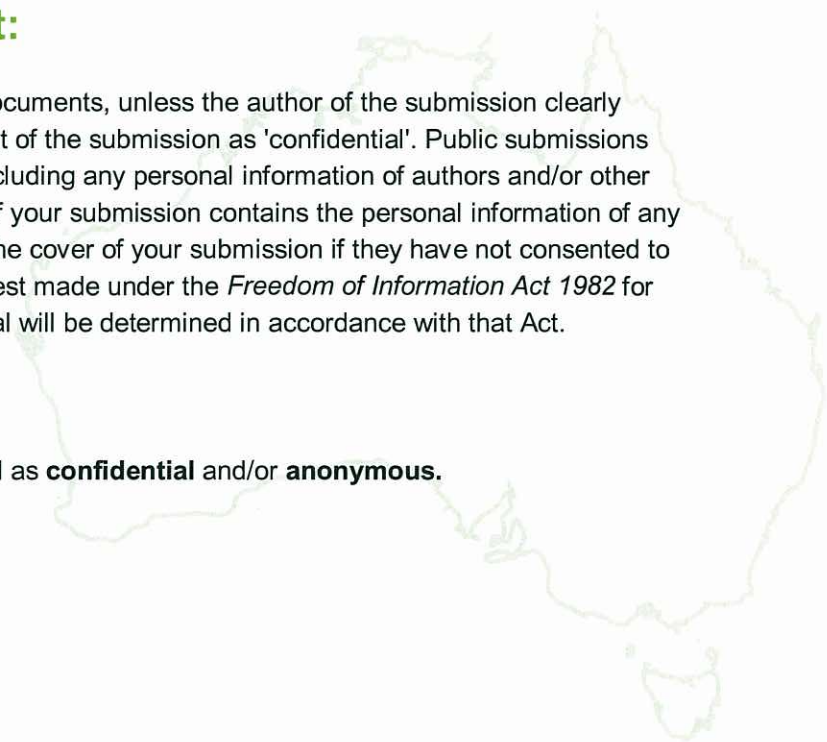
Date:

10 September 2008

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I **do not** want this submission to be treated as **confidential** and/or **anonymous**.



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Submission to the

Carbon Pollution Reduction Scheme Green Paper

10 September 2008

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1.0 Executive Summary

Leighton Holdings and its subsidiary companies welcome the opportunity to respond to the Carbon Pollution Reduction Scheme (CPRS) Green Paper. We agree with the overarching objective of the CPRS to reduce Australia's carbon pollution while building long-term economic prosperity in a lower carbon economy.

As a successful Australian-based company, large employer and big energy user, the Leighton Group is keen to work with the Government to ensure the design of the CPRS meets Australia's economic and environmental goals.

However, as Australia's largest mining and construction contractor, we are concerned that elements of the current preferred CPRS model, combined with a misalignment with the National Greenhouse and Energy Reporting System (NGERS), will impose unduly onerous reporting obligations and permit acquittal liabilities on contractors. Contract mining is a unique Australian service industry but the NGERS and the CPRS have been modelled on owner-operated facilities. We believe that greater reductions in carbon emissions can be achieved by imposing scheme obligations on project owners, rather than service providers.

The Leighton Group makes the following recommendations:

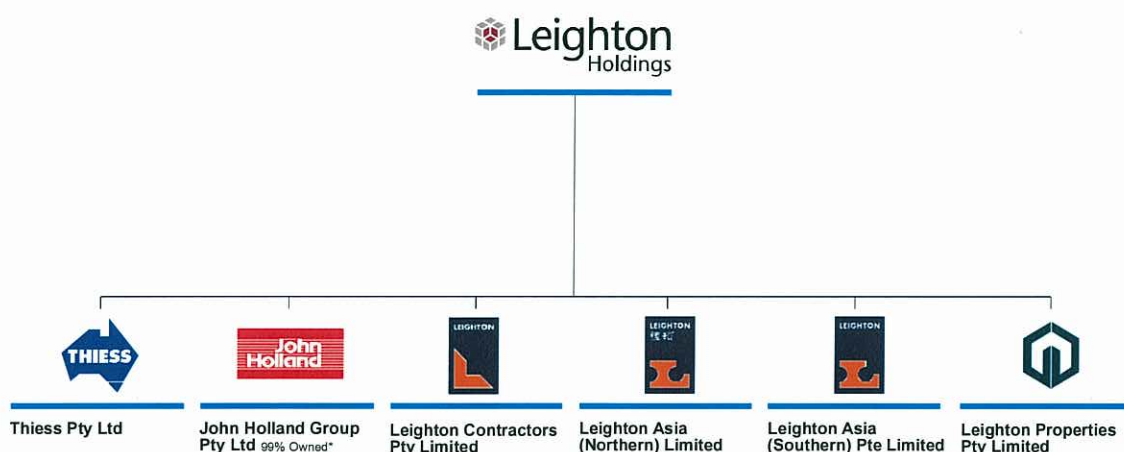
- Amend the NGER Act and draft the CPRS legislation to explicitly recognise mine owners as the facility operator on mine sites, with responsibility for reporting on energy use, energy production and greenhouse emissions and for acquitting carbon permit liabilities.
 - The alternative would be to allow parties on a mine or major construction project to commercially negotiate 'operational control'.
- The CPRS should differentiate between mine owner liabilities for emissions directly associated with the resource (ie: fugitive emissions and black coal sold to small emitters) and operator liabilities for emissions produced during extraction and haulage of the resource.
 - Alternatively, the emission liability threshold for facilities of 25kt CO₂-e should exclude fuel-generated emissions to avoid unnecessary trading and administration burden for marginal emitters.
- Transition arrangements should allow for the inability of existing contracts to pass through costs associated with the CPRS.
- Equitable transitional treatment of fuel cost offsets should be given to on-road and off-road transport.
 - Mining and construction should also be included, given their major contribution to rural and regional Australia.
- Compensation provided to Emissions Intensive Trade Exposed industries should be available to the entity with CPRS liabilities.

- Liability for fuel should be maintained upstream at the refinery or terminal gate as it maximises coverage and simplifies the administration of the CPRS.

The Leighton Group also has a substantial services business, which includes waste management. We are concerned the preferred CPRS model will force our owner operated landfill businesses to close. Thiess Services Pty Ltd has made a separate submission to the Green Paper.

2.0 Background

Leighton Holdings Limited is the parent company of Australia's largest project development and contracting group. The Leighton Group includes Leighton Contractors, Thiess, John Holland, Leighton Properties, Leighton International and Leighton Asia. The Group employs more than 37,000 people around the globe, including nearly 22,000 in Australia – about half of whom work on construction, mining and services projects in rural and regional Australia.

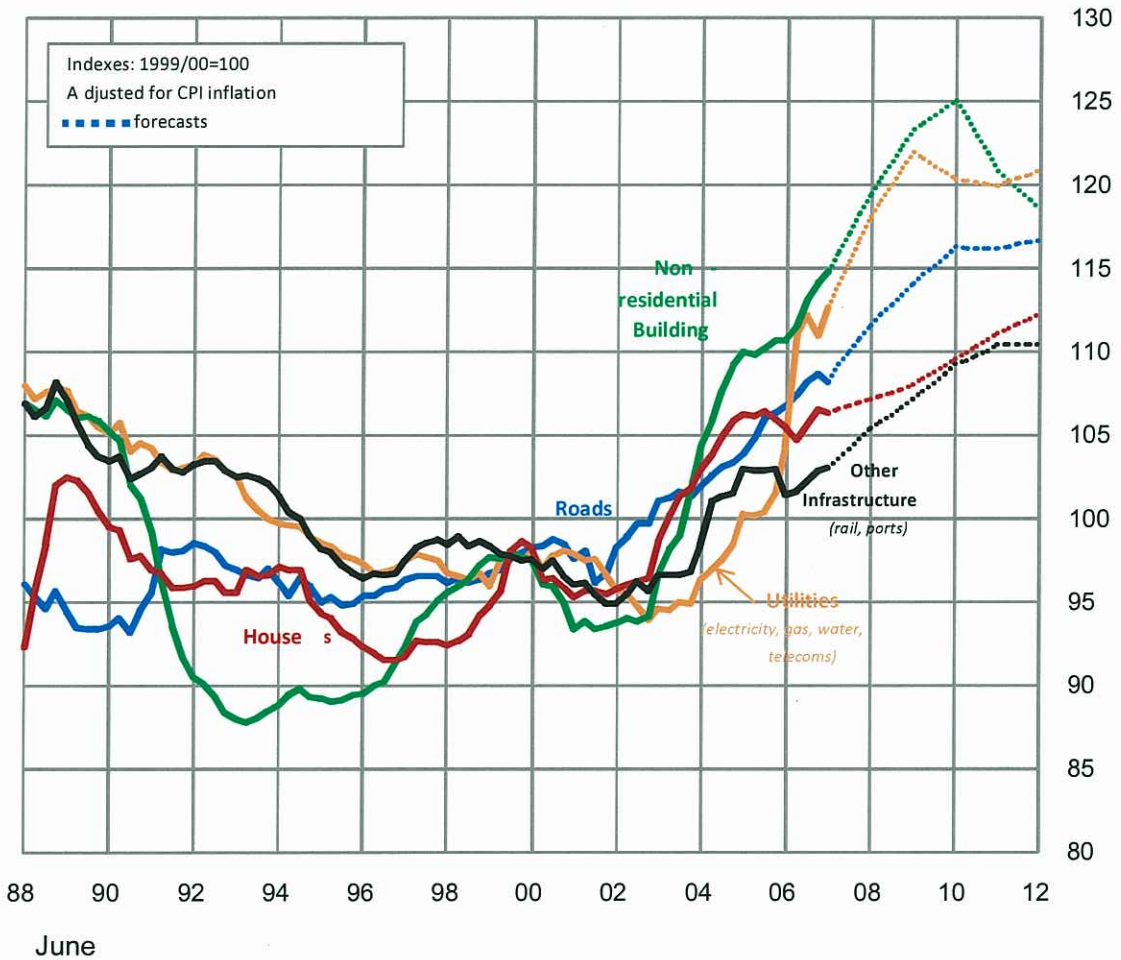


Given that protection of the environment is a core value for the Leighton Group, we actively work to reduce our carbon footprint. As service providers, we continually seek fuel efficiencies within the constraints of our clients' requirements. Two of our operating companies, Leighton Contractors and Thiess, are part of the Greenhouse Challenge Plus and Energy Efficiency Opportunities Assessment Program. We are already collecting the information required under the NGER Act and support its objectives to provide a streamlined, accurate and transparent emissions reporting system which maintains commercial confidentiality.

The energy and emission profile of the Leighton Group's activities is dominated by the use of diesel, primarily on contract mining projects. At a carbon price of \$20 per tonne of CO₂-e and based on our emissions in 2006-07 (excluding liabilities for fugitive emissions from landfills and open cut mines), the permit cost to the Group would be \$33.4 million. We expect this liability in the future would be significantly more, given NGER requires more detailed reporting of greenhouse gas data. We estimate almost 98 per cent of our emissions are attributable to fuel, with at least 19 contract mining projects reaching the 25kt CO₂-e 'facility' threshold based on diesel usage alone. However, if the Leighton Group was liable for fugitive emissions from landfills and open cut mines, we estimate our permit cost would increase by almost 400%.

Our current order book includes a number of large infrastructure projects, but their energy and emissions profile do not reach the 'facility' level. We believe the CPRS will impact on our infrastructure projects primarily through rising input costs associated with a carbon price.

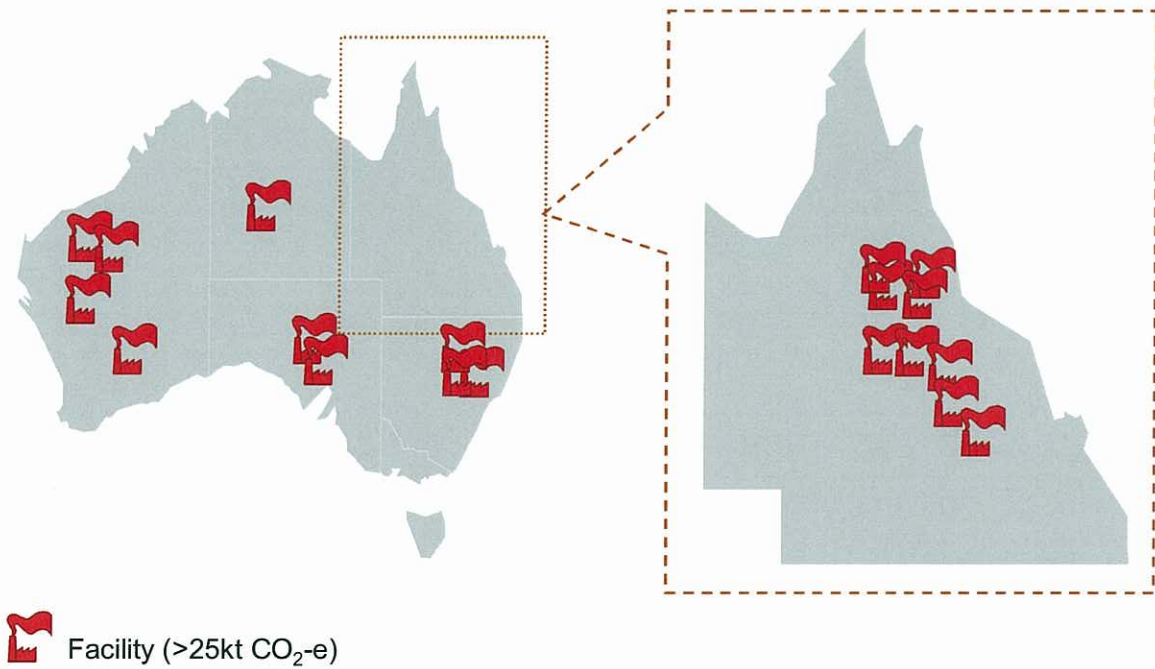
Real Construction Costs by Sector



Source: ABS & Macromonitor

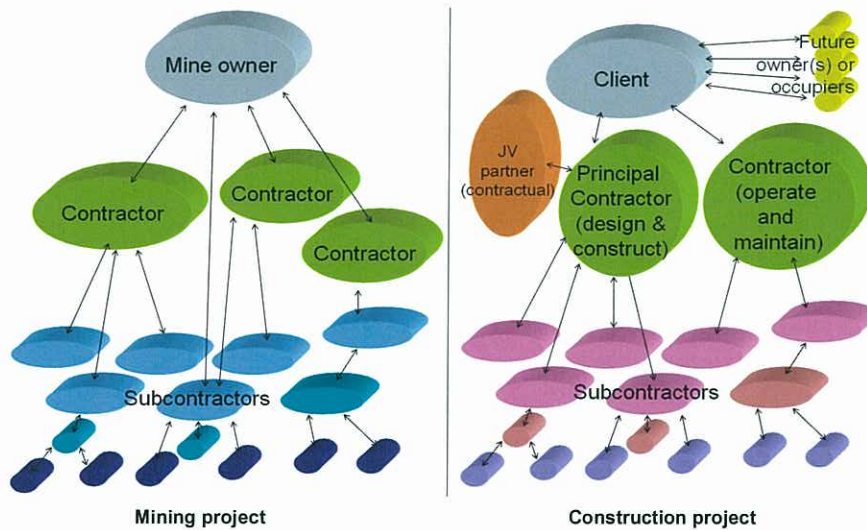
Our submission focuses on the direct impact of the preferred trading scheme model on our contract mining projects.

At least 19 Group mining projects reach “facility” threshold



Contracting often includes a set of complex arrangements for the provision of services by a number of participants to the client. Projects can involve the owner, joint venture partners, contractors and many sub contractors. While there are broadly seven different forms of contractual models in mining and 17 in infrastructure every contract is unique and varies from these broad models. The more intricate forms are usually associated with more complex projects.

Contracting is Complex



Source: Australian Constructors Association

Forms of Contract Mining

Risk transferred (to contractor)	Risk shared (with contractor)	Risk acceptance (by client)
<ul style="list-style-type: none"> - Lump sum, schedule of rates 	<ul style="list-style-type: none"> - Alliance – Project costs reimbursed on open book basis - Payment of fixed costs and variable cost schedule of rates - Partnering – “risk transfer” combined with commitments to shared objectives - Cost Reimbursable Performance Incentive (CRPI) 	<ul style="list-style-type: none"> - Cost reimbursable - Fee for service

All could be undertaken in joint venture

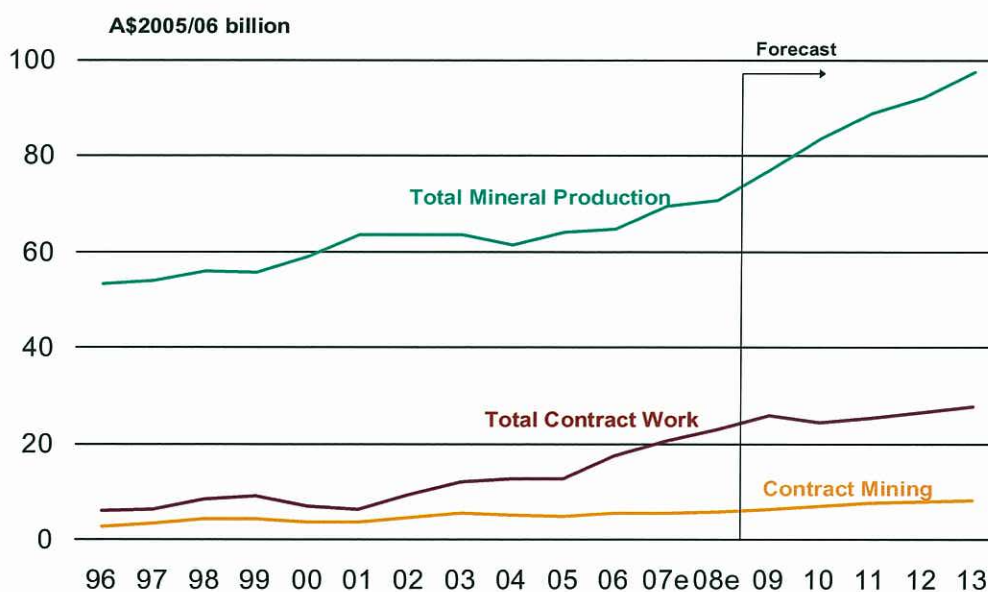
Forms of Construction Contracts

Risk transferred (to contractor)	Risk shared (with contractor)	Risk acceptance (by client)
<ul style="list-style-type: none"> - Fixed price - Lump sum - Guaranteed Maximum Price (GMP) - Hard dollar - Schedule of rates - Public Private Partnership/BOOT - EPC/Turnkey 	<ul style="list-style-type: none"> - Alliance - Performance incentive - Warranted maximum price with share of variance - Construction management - Staged exclusive negotiation leading to GMP 	<ul style="list-style-type: none"> - Cost reimbursable - Project management - Managing contractor - Engineering Procurement and Construction Management (EPCM) - Fee for service

All could be undertaken in joint venture

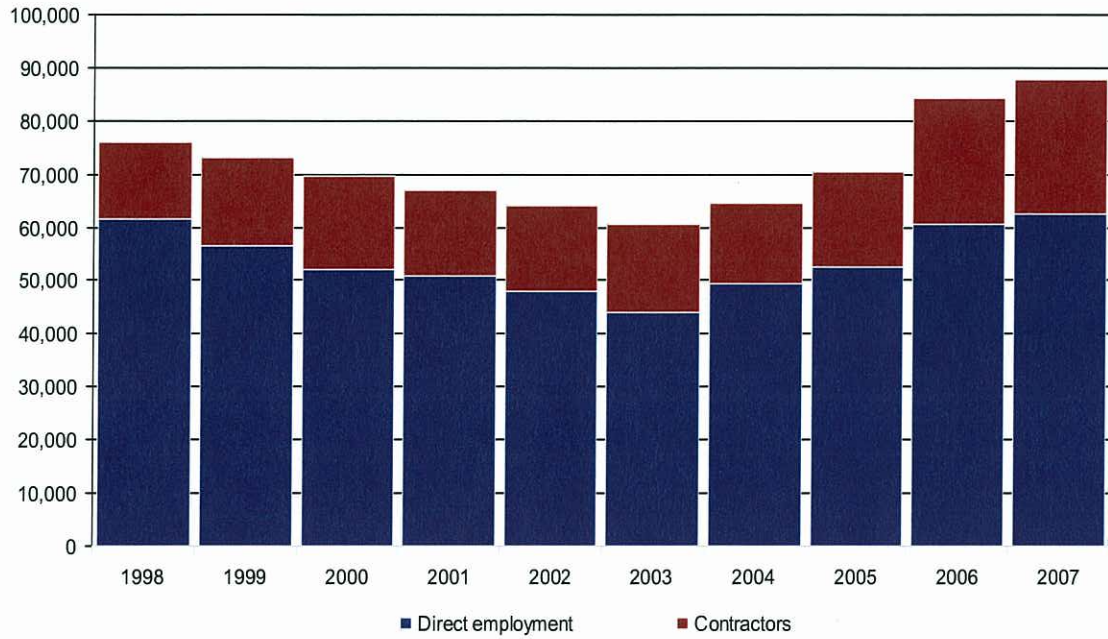
Contract mining is largely unique to Australia and the share of mining done by contractors is increasing. Contract mining has grown from 18 per cent of total mining in 1997/98 to 28 per cent in 2006/07. The Minerals Industry Survey in 2007 showed that the industry had 62,740 direct employees and 25,225 contractors. There are few other countries where mining is undertaken by contractors as mines are generally owner-operated – so there is no international precedent for treatment of contract mining in emissions trading schemes.

Contractors account for 30% of mining sector work



Source: BIS Shrapnel Mining in Australia 2008

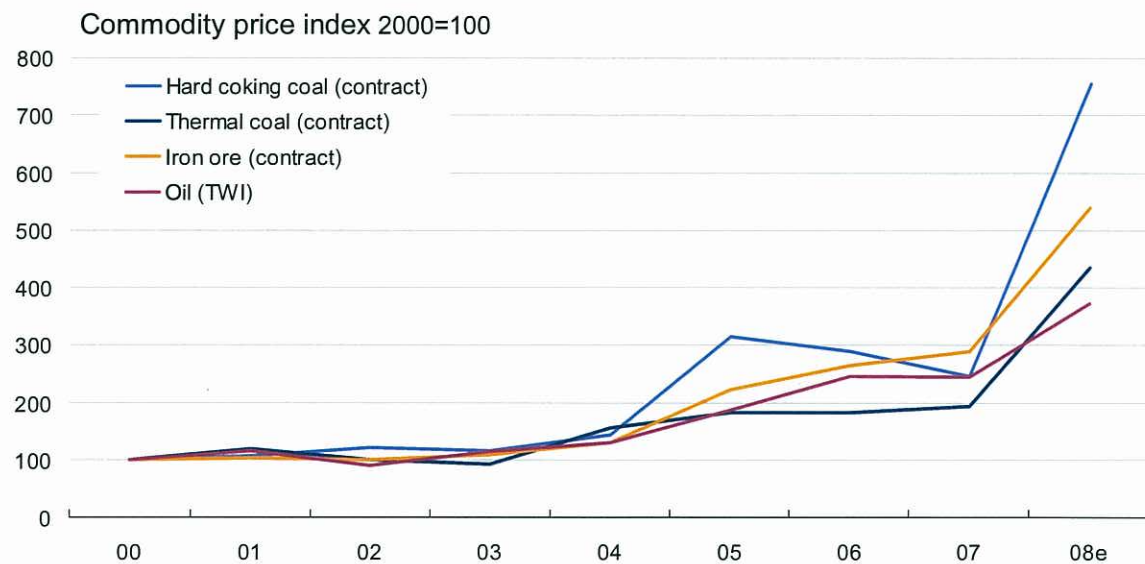
Employment in the Minerals Industry



Source: Minerals Council of Australia

As a service provider the margins for contract miners are low and do not fluctuate significantly with changes in commodity prices. Contractors do not have the capacity to absorb additional costs, nor sufficient length of tenure when managing an orebody to make major capital investment in infrastructure such as draglines which cost more than \$100 million each. This is especially the case in the current climate of rapidly rising material and input costs.

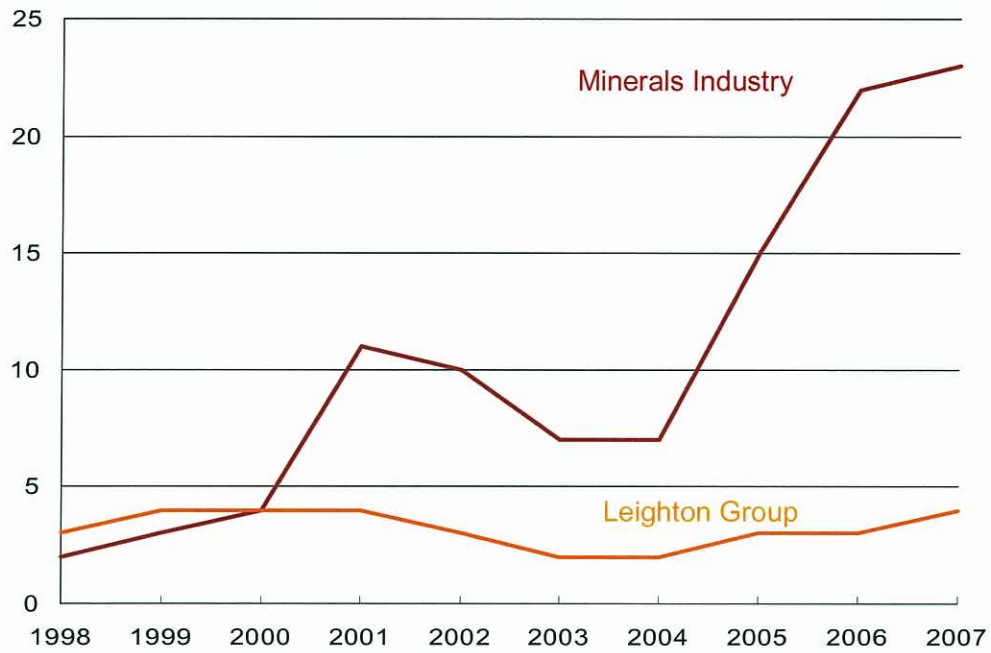
Australian Mining Market



Source: ABARE, Bloomberg

Mine Owners have the money to invest in carbon reduction

Profit margins (%)



Source: Minerals Council of Australia, Leighton Holdings Limited

The relationship between a mine owner and a Leighton operating company can vary from providing a limited service to a portion of a mine operation to being the overall manager of the mine site. Where there are multiple contractors on site, the Leighton operating company may have no contractual or legal relationship with other contractors which will deal directly with the mine owner. While the Leighton operating company may introduce its own policies for safety, environmental and operations, these policies must be compatible with the overarching policies that the mine owner has established for the entire facility and their business. A mine owner has the right to approve the operator's policies and can require an operator to change its policies to comply with the owner's requirements, even in situations where the Leighton operating company may be the registered mine manager.

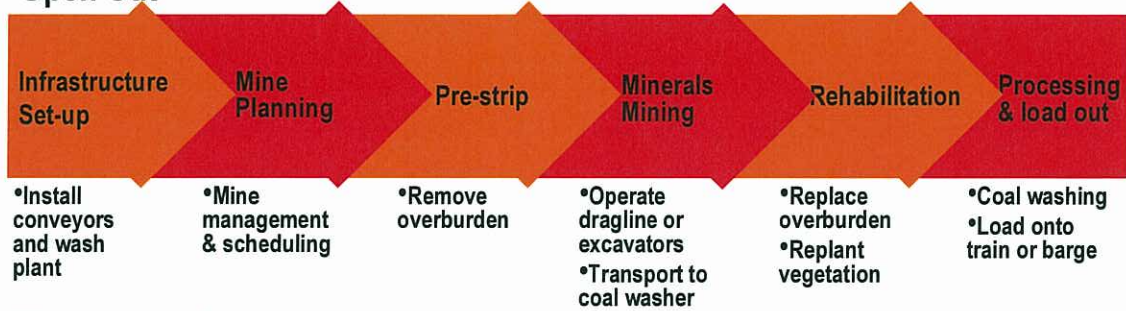
Typical role of a contractor in the mining sector

	Owner Operator	Traditional Contract Miner	Full Services Contracting
Contractor Activity	<ul style="list-style-type: none"> - Limited to infrastructure set-up 	<ul style="list-style-type: none"> - Pre-strip - Mining - Rehabilitation 	<ul style="list-style-type: none"> - Infrastructure set-up - Mine planning - Pre-strip - Mining - Processing & load out - Rehabilitation
Delivery System	<ul style="list-style-type: none"> - Design & construct - Lump sum 	<ul style="list-style-type: none"> - Schedule of rates - Lump sum 	<ul style="list-style-type: none"> - Alliancing - Schedule of rates per tonne delivered - Schedule of rates for some components
Investment by Contractor	<ul style="list-style-type: none"> - Nil 	<ul style="list-style-type: none"> - Plant & equipment - Working capital 	<ul style="list-style-type: none"> - Plant & equipment - Working capital - Investment stake in mine
Skills Required by Contractor	<ul style="list-style-type: none"> - Construction 	<ul style="list-style-type: none"> - Earthmoving/ Mining skills 	<ul style="list-style-type: none"> - Construction - Mine planning - Earthmoving/Mining skills - O&M

Regardless of the contractual arrangements, the miner owner has the most influence on the use of energy at a mine. The most important determinant of fuel usage is the mine plan, that is, determining in what sequence the mine will be developed and the quantities that will be mined.

The mining process

Open Cut



Underground

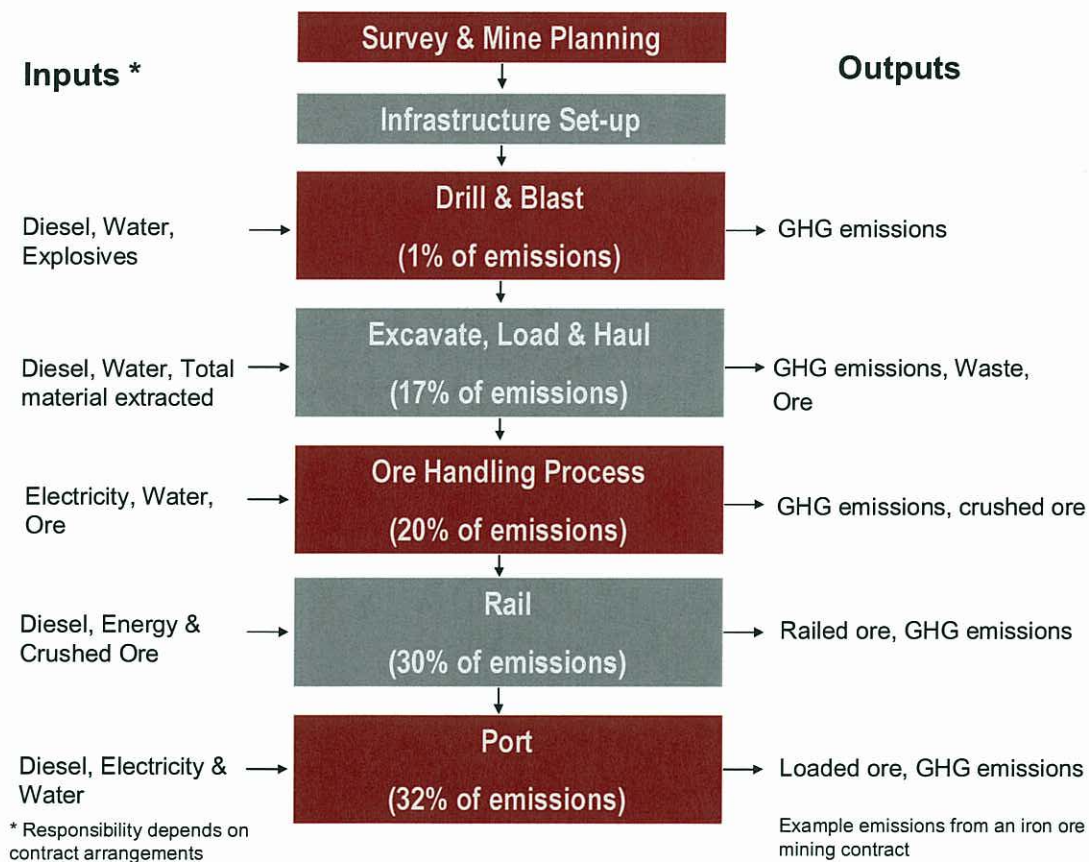


The mine owner is responsible for:

- Determining the life of the mine.
- Approving the mine plan, taking into consideration the desired life of the mine and the product mix required for customers.
- Determining the methods and contract structures to mine the product.

The mine plan would not necessarily be prepared with the objective to minimise the amount of energy used during the mining process if the contract miner bears the carbon liability.

Mining is a small part of the emissions profile in the resources sector



In addition the mine owner is often the entity exposed to fuel costs. One of the trends in mining is that the mine owner is increasingly purchasing fuel and providing it to the contractor. For the Leighton Group the share of fuel provided by the mine owner on our Australian projects was approximately 60 per cent in 2007.

Leighton operating companies often work with the fixed infrastructure determined or provided by the mine owner. The life of a fixed investment would usually exceed the term of the contract. A decision, for example, to install a large scale gas, solar or wind power station to reduce greenhouse gas emissions would generally be made by the mine owner. Similarly, major plant modification for energy efficiency reasons would be a capital investment decision for the mine owner.

3.0 Issues with Green Paper

The Green Paper states “the objective of the Carbon Pollution Reduction Scheme is to meet Australia’s emissions reduction targets in the most flexible and cost effective way; to support an effective global response to climate change; and to provide for transitional assistance for the most affected households and firms”. We believe the impact of the preferred CPRS design on service providers to the mining and, to a lesser extent, construction industries fails the test against the stated assessment criteria of environmental integrity, economic efficiency, minimisation of implementation risk, accountability and transparency and fairness.

Our assessment is the preferred model has the potential to:

- Impose more red tape and unnecessary costs on the Leighton Group,
- Provide the public with inaccurate information about emissions on mine sites,
- Allow those with the most ability to cut pollution in the mining sector to escape liability, and
- Reduce the opportunities for cutting carbon pollution.

The major problem is a technical one. The definition of ‘operational control’ in the NGER Act does not apply logically or fairly to the mining sector, where a third of work is undertaken by contractors. This has the potential to draw service providers into the trading scheme – rather than properly directing obligations to reduce emissions towards those best able to do so and those benefiting most from the mining industry.

3.1 Operational Control

The Green Paper considered whether operational or financial control was the best framework for allocating obligations under the Scheme. The Green Paper stated that in most cases a single entity would own and operate a facility so there was no difference between financial and operational control. The Green Paper also recognised that selecting an entity would be more complex where operational and financial controls are separated or where the facility is owned by a number of entities. The Green Paper preferred position is that the obligation should be for entities with operational control, based on the NGER approach. The Green Paper acknowledged that with respect to forestry and upstream fuel, further consultation and analysis would be undertaken on the definition of liable entities.

The Leighton Group is concerned about the liable entity in relation to mining. The Leighton Group considers that the mine owner is best placed to report on energy use and greenhouse emissions and to have CPRS liability. The mine owner initiates the mine development, decides who will work on the project and is a

constant for the duration of the mine. The mine owner has greatest influence on energy use and emissions, owns and markets the product, and is best placed to collect data from multiple contractors. The mine owner approves the mine plan, determining where the minerals will be mined, where waste will be dumped and the rate of extraction – and ultimately energy usage and carbon pollution.

The Leighton Group considers that the mine owner needs to be recognised explicitly as the liable entity in the NGER Act and the CPRS in relation to the mining sector.

However, if the Government decides that the NGER Act and CPRS will not explicitly recognise the mine owner as the key entity, the Leighton Group would suggest that the CPRS should provide the opportunity for entities to determine amongst themselves which one might be most appropriate to be the facility operator. There are often a number of commercial, contractual and other reasons why entities might prefer to agree which party might be best suited to be the facility operator.

The Leighton Group suggests an alternative would be to ensure the NGER Act and CPRS allow parties to commercially negotiate liability.

3.2 Fugitive methane emissions and emissions from black coal combustion by small emitters

The Leighton Group is concerned that the Government proposes to include fugitive methane emissions from coal mines in the CPRS ahead of an accurate form of measurement. We support submissions from the minerals industry to develop a sound science-based methodology for estimating fugitive emissions from open cut mines and to phase in CPRS coverage of fugitive emissions.

However, if fugitive emissions are included in the scheme from its introduction, the Green Paper has sought to simplify the CPRS by making the facility operator the key entity responsible for fugitive methane emissions from coal mines and the downstream emissions of small coal users. It is the mine owner, not contractors, who is best placed to report on fugitive emissions from open cut mines and on the energy content of coal sales to small emitters. The mine owner has control and ownership responsibility over the resource before, during and after contractors have been on site. Normally contractors have no information on the state of fugitive emissions from open cut mines, nor do they have the legal relationship to require mine owners to provide such information or the capacity to pass on the costs to collect such information.

Even using the most basic method of estimating fugitive emissions based on the amount of coal we have extracted, at a carbon price of \$20 per tonne of CO₂-e we estimate the permit cost to the Leighton Group would be approximately \$40 million if we were liable for fugitive emissions from open cut mines. We can't estimate the liability for downstream coal sales as we have no entitlement to that information from our clients.

The Leighton Group believes the CPRS should differentiate between mine owner liabilities for emissions directly associated with the resource and operator liabilities for emissions produced during extraction and haulage of the resource.

3.3 Fuel liability

The Green Paper has a preferred position to impose scheme obligations for emissions from petroleum fuels with suppliers covered by the fuel excise and customs duty systems. **The Leighton Group supports this preferred position for upstream fuel liability as it maximises scheme coverage, reduces compliance costs and simplifies the administration of emissions liability.**

The Green Paper has indicated that consideration will be given in the first year of the scheme for large fuel users to opt to take the liability. **The Leighton Group supports a scheme which gives large fuel users the option to take the liability from the upstream suppliers.**

3.4 Facilities and emissions threshold

The Green Paper has proposed that "the emissions threshold for direct obligations under the scheme would apply to entities with facilities which have direct emissions of 25,000 tonnes of carbon dioxide equivalent a year or more". This implies that emissions less than 25kt CO₂-e are not considered sufficiently material for a corporation to incur the financial and administrative burden to acquit the liabilities. However one outcome of upstream liability is that big energy users whose emissions are largely due to fuel use will be required to purchase and trade carbon permits for residual emissions that may be well below the 25kt CO₂-e threshold.

Diesel and petrol use accounts for almost 98 per cent of the Leighton Group's energy use and operational emissions. Less than one per cent is attributable to other sources such as electricity and explosives. The preferred CPRS model would require Leighton Holdings to establish a carbon permit trading capability for about two per cent of the Group's direct emissions plus emissions that are not related to our operations (such as fugitive emissions, downstream emissions of small coal users and potentially emissions from other contractors or sub

contractors on the same site). Consistent with the Green Paper goal of simplicity and cost effective administrative burden, the Leighton Group suggests that the scheme should work on a net reporting basis.

The Leighton Group considers that facilities with net (non-fuel) emissions of less than 25kt CO₂-e per annum should not be included in the CPRS.

3.5 Reporting

The Green Paper seeks feedback on whether the scheme should provide for the publication of reported information to the facility level. **Consistent with our submissions to the Government on NGERs, the Leighton Group considers that facility-level reporting would be commercially sensitive.**

3.6 Pass Through

The Green Paper seeks comment on the implications that CPRS might have on existing contractual arrangements and in particular the capacity to pass costs on to the client. There are two types of costs that will come from the CPRS. The first is the direct cost which can be identified with the purchase of permits. The second is the indirect costs which are embedded in products and services due to higher transport, energy and administrative costs. Some contracts do have a capacity to pass on unforeseen direct costs such as generated from the CPRS. Others are fixed price and provide little scope to pass on unforeseen costs. Indirect costs would be more difficult to pass through.

With more than 40 per cent of our Australian contracts ending in or after 2010, the Leighton Group is still reviewing its capacity to pass on costs associated with the CPRS. It seems likely that we will be unable to pass on the CPRS costs in a number of cases. This may have serious financial implications for the Group, at a time when the costs of materials and services are already rising strongly across construction sectors. While it is difficult to ascertain exact impacts without Treasury modelling, we believe three key inputs to our business are likely to be significantly affected by the CPRS – electricity, steel and cement. **To address this transitional problem the Leighton Group would like to continue to consult with the Government to ensure that businesses do not incur unintended costs.**

3.7 Rural and Regional

The Green Paper is mindful of the adjustment costs facing Australian households and businesses. The Government has committed to cut fuel taxes on a cent for cent basis to offset the initial price impact on fuel associated with the introduction of

the CPRS. This will be extended to agriculture and fisheries to assist rural and regional areas.

The Leighton Group believes that mining and construction activities have a significant impact on rural and regional Australia. Mining is predominately conducted in rural and regional Australia and is the major employer in many areas. Likewise the construction of road, rail, ports and other infrastructure have a major impact on the economic activity of regional Australia. According to the Department of Resources, Energy and Tourism, the mining industry over the last four decades has built 26 towns, 12 ports, 25 airfields and over 2000 kilometres of railway. In remote areas, minerals and construction industries are often the sole provider of social infrastructure such as health and education, and the benefits from these endure well past the end of their activity.

For example, more than 89,300 people are estimated to live and work in Queensland's Bowen Basin – many are employees and contractors on the 34 operational coal mines, including about 2200 people employed by Leighton Group companies on 17 coal mining projects.

The minerals industry is a major provider of employment and training of indigenous communities. Leighton subsidiaries seek to provide opportunities for indigenous employment. For example, Leighton Contractors invested in a 50 per cent interest in the indigenous contracting company, Ngarda Civil and Mining, based in the Pilbara region of Western Australia. The company generates more than \$120 million in annual revenues and more than half of Ngarda's 390 employees are indigenous.

Current Mining Projects in Australia



The Leighton Group suggests that including mining and construction in the fuel rebate arrangement for agriculture and fisheries would be at least as effective in pursuing the government’s objective of assisting rural and regional Australia but also be more equitable across industry sectors.

The Green Paper also proposes that on-road transport will be excluded from any increase in fuel costs related to CPRS. The Green Paper does not provide any justification for differentiating between on-road and off-road use of fuel. **The Leighton Group would suggest for equity and consistency, off-road and on-road transport should both be provided with carbon cost offsets. With regard to rural and regional Australia, mining and construction should also be included in the fuel offset scheme.**

3.8 Emissions Intensive Trade Exposed (EITE)

The Leighton Group supports the Government’s commitment to providing transitional assistance to EITE industries. However we agree with the Minerals Council of Australia, the Australian Coal Association and the Business Council of Australia that the Green Paper’s preferred metric used for determining EITE status is not appropriate.

The resources sector is the most internationally competitive and most export oriented sector of the Australian economy. The capacity to pass on costs is limited by the extent of competition from other countries' supplies. The mining sector represents almost eight per cent of the Australian economy and accounts for almost 50 per cent of export revenue.

Regardless of the metric used, the Leighton Group believes the previously outlined problems with operational control will lead to anomalies if the resources sector is allocated free permits. There is potential for assistance to be provided to mine owners even though they may not have liability to acquit permits at facilities where a contractor is deemed to have operational control.

The Leighton Group considers that service providers with CPRS liabilities operating in an EITE industry should be entitled to transitional compensation, if it is granted.

3.9 Waste

Thiess Services, a wholly owned subsidiary of Thiess Pty Ltd, is making a separate submission on issues related to waste, which Leighton Holdings endorses.

Significantly, at a carbon price of \$20 per tonne of CO₂-e Thiess Services estimates the permit cost would be a \$5.35 million annually, plus \$42.3 million based on the volume of waste received at its landfills to date. This cost is more than 100% of Thiess Services' annual profit and would likely result in the closure of the Swanbank and Springmount operations in Queensland and the loss of about 50 jobs. There are also two broader issues for the Government to consider. First, security of waste disposal is a critical public health issue and closure of these facilities means alternatives would need to be found. Second, the closure of mature landfill sites means the loss of innovative carbon capture solutions. At Swanbank the carbon capture system not only reduces waste's carbon footprint, but the gas is used for electricity generation.

The Leighton Group considers coverage of the waste sector should be deferred until fugitive landfill emissions can be measured accurately and legacy waste emissions should be excluded from the scheme.

4.0 Summary of key Leighton Holdings proposals

The Leighton Group proposes that:

- Mine owners should be the liable party for the NGER and CPRS.
- Mine owners should be responsible for fugitive emissions and liabilities for sales to coal to small emitters.
- If contractors are deemed liable for the NGER and CPRS:
 - Commercial parties to a mine or major construction project should be allowed to determine the most appropriate entity to be liable for emissions.
 - The emission liability threshold for facilities of 25kt CO₂-e should exclude fuel-generated emissions to avoid unnecessary trading and administration burden for marginal emitters.
- Mining and construction should be covered by the fuel carbon cost offset scheme because of their contribution to rural and regional Australia and for consistency with the on-road offset.
- Consultations need to continue with government on capacity of existing contracts to pass through CPRS costs.
- CPRS liability for fuel should remain upstream.
- Coverage of the waste sector should be deferred until there is a more accurate method of measuring fugitive emissions.
 - Legacy waste emissions should be excluded from the CPRS.