AUSTRALIAN CONSERVATION FOUNDATION

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# ACF Submission
# Proposed changes to the Safeguard Mechanism

The Australian Conservation Foundation (ACF) welcomes the opportunity to provide a submission to the Department of Climate Change, Energy, the Environment and Water about proposed changes to the Safeguard Mechanism.

## *Introduction*

ACF is Australia's national environment organisation. We are over 700,000 people who speak out for the air we breathe, the water we drink, and the places and wildlife we love. We are proudly independent, non-partisan and funded by donations from our community.

ACF considers that Australia and the world face an unprecedented climate and mass extinction crisis caused first and foremost by digging up and burning fossil fuels like coal, oil, and gas. ACF has long advocated for a national approach to reduce climate emissions in line with the science-based temperature goals that Australia committed to under the Paris Agreement.

ACF welcomes the review of the Safeguard Mechanism and the Australian government's commitment to turn the Safeguard Mechanism into an emissions reduction policy that will assist in achieving Australia's climate commitments. That includes 43% emissions reduction on 2005 levels by 2030, future updates to Australia's Nationally Determined Contribution under the Paris Agreement (e.g., Australia's 2035 target once set) and net zero by 2050.

The Safeguard Mechanism has provided a free pass to Australia's largest polluters for many years. It has been labelled a "toothless tiger" and a "do nothing policy" yet it offers a policy architecture that can be turned into an effective policy tool.

Currently, ~215 facilities, which account for 28% of Australia's annual emissions, have virtually no emissions reduction requirements guiding their transition to cleaner operations. A predictable phase down of Safeguard Mechanism baselines can turn it into a useful tool, helping to reduce industry emissions in a manageable way, spark investment in clean solutions and ultimately make Australian industry more competitive in a global market that puts a premium on products with a low carbon footprint. However, as with many technical policies, the devil is in the detail, and in this case the detail matters. ACF offers our views below.

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## 1. Issues not addressed by the Consultation Paper

### Coverage threshold

The Australian government's *Safeguard Mechanism Reforms: consultation paper* states that "The current coverage threshold of 100,000 tonnes of scope 1 (direct) carbon dioxide equivalent or CO2-e emissions each year will remain in place under the reformed scheme." However, ACF recommends this threshold is lowered to 25,000 tCO2-e.

Lowering the threshold to 25,000 tCO2-e would enhance the reach and impact of the Mechanism. The lower threshold would more adequately cover industrial emissions that are currently going unregulated. The business sector, including the Business Council of Australia (BCA), have supported lowering the threshold to 25,000 tCO2-e.[1]

To give an indication of the additional emissions reduction that could be achieved with a 25,000t CO2-e threshold, the Clean Energy Regulator reported in response to a Senate estimates question that the total amount of scope 1 and scope 2 emissions reported under the *National Greenhouse and Energy Reporting (NGER) Act 2007* for facilities with total emissions between 25,000–100,000 tCO2-e in 2018–19 was 24,482,137 tCO2-e.[2]

ACF understands that lowering the threshold would incorporate facilities from sectors already covered under the Safeguard and would level the playing field. These sectors include:

- Air and Space Transport
- Cement and Lime Manufacturing
- Coal Mining and Gas Supply
- Iron and Steel Casting
- Iron Ore Mining, and Oil and Gas Extraction
- Pharmaceutical and Medicinal Product Manufacturing
- Rail Freight Transport
- Sewerage and Drainage Services
- Urban Bus Transport (Including Tramway)

[1] Business Council of Australia. (2021). *Achieving a net zero economy.* Retrieved 9 September 2022 from: https://d3n8a8pro7vhmx.cloudfront.net/bca/pages/6612/attachments/original/1633693581/BCA_Achieving_a_net_zero_economy_-_9_October_2021.pdf?1633693581

[2] Clean Energy Regulator. (30 October 2020). *Question No.: 91, Environment and Communications Legislation Committee Answers to Questions on Notice, 2020–2021 Budget Estimates. Retrieved on 9 September from: https://www.aph.gov.au/Parliamentary_Business/Senate_estimates*

It would also incorporate sectors with mid-tier emissions which would benefit from a signal to start working on the deep cuts needed to get to net zero by 2050 and beyond.

*Recommendations*

- The threshold should be reduced to 25,000 tCO2-e per annum to capture additional (mid-tier) emitting facilities, and to ensure that the Safeguard Mechanism has the largest impact on reducing emissions. If this will not be considered in the first iteration of Safeguard Mechanism reforms, it should be considered as a priority for the next review.
- The threshold of 100,000 tCO2-e should not represent a floor for emissions reductions. Facilities should not "drop out" of the scheme if they reduce their emissions below the threshold.

## Treatment of the power sector

Electricity generators are covered by the Safeguard Mechanism, but facilities in the power sector are not treated like other facilities. Instead, they are covered by a sectoral baseline, which covers the emissions of the entire sector. This means that renewable energy generators are combined with coal and gas generators under one baseline.

The sectoral baseline is 198 million tonnes CO2-e (MtCO2-e), which is the high point of emissions over the FY 2010–14 reporting period. In FY 2020-21, reported sectoral emissions were approximately 164 Mt, well below the sectoral baseline.[3]

The fact that reported emissions are well below the baseline does not mean that emissions from many electricity generators are not significant, just that their special treatment through a sectoral baseline provides cover for the most polluting generators. Under this arrangement, coal and gas generators have no incentive to reduce emissions and do not pay a penalty or buy carbon credits.

The most effective way to reduce emissions from the electricity sector is through the phased closure of fossil fuel generators and by accelerating the transition to 100% renewable energy including through supporting infrastructure such as transmission. This requires significant structural changes that are best effected through the Powering Australia Plan.[4]

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[3] CMI Research prepared by Reputex Energy. (2022). *Potential Futures for Australia's Safeguard Mechanism.* Retrieved on 9 September 22 from: https://carbonmarketinstitute.org/app/uploads/2022/06/Potential-futures-for-Australias-Safeguard-Mechanism.pdf

[4] Commonwealth Government. (2021). *Powering Australia*. Retrieved on 9 September 2022 from: https://www.energy.gov.au/government-priorities/australias-energy-strategies-and-frameworks/powering-australia

ACF does not want to see the Mechanism encouraging facility-level improvements that improve emissions intensity but prolong the life of fossil fuel generators – as we saw when Delta attempted to upgrade turbines at Vales Point coal-fired power station.[5] As such, we do not recommend that the Safeguard captures power generators.

However, it is important the Clean Energy Regulator (CER) prevents leakage of Safeguard facilities into the electricity sector. ACF is concerned that operational boundaries may be drawn in such a way to allow for some coal mines and facilities adjacent to generators to fall within the sectoral baseline.

To ensure effectiveness of the overhauled Safeguard Mechanism, ACF considers that there is need for the CER, or another agency such as the Climate Change Authority (CCA), to conduct an audit of all electricity generation facilities to determine whether any include operations that would be better regulated under the Mechanism.

*Recommendations*

- The electricity sectoral baseline should align with the Step Change Scenario in the *Australian Energy Market Operator's* 2022 Integrated System Plan.[6]
- The CER or CCA should conduct an audit of all electricity generation facilities to determine whether any include operations that would be better regulated under the Safeguard Mechanism.

## Addressing scope 3 emissions

ACF understands that the intention of the enhanced Safeguard Mechanism is to continue to focus only on scope 1 (direct) emissions. However, given the enormity of Australia's scope 3 emissions, we have a responsibility to address these emissions, and to start with transparent tracking and reporting. For example, ACF has recommended that the Climate Bill 2022 be amended to require scope 3 emissions to be tracked and reported in annual climate change statements to Parliament.

*Recommendation*

- The Australian government conducts a review to consider how scope 3 emissions are regulated, noting that it may not be possible to bring scope 3 emissions into the Safeguard Mechanism.

[5] Delta Electricity. (2020). *Media Release*. Retrieved on 9 September 2022 from: https://www.de.com.au/ArticleDocuments/10283/Delta%20withdraws%20from%20UNGI.pdf.aspx

[6] AEMO. (2022). *2022 Integrated System Plan*. Retrieved on 9 September 2022 from: https://aemo.com.au/en/energy-systems/major-publications/integrated-system-plan-isp/2022-integrated-system-plan-isp

However, following a review there may be potential to include scope 3 emissions in phase 2 of the Safeguard Mechanism (2026–30).

### Role of the Climate Change Authority (CCA)

The Australian government has committed to reinvigorate the CCA. As an independent body, the CCA provides expert advice to government on a range of matters including potential future emissions reduction targets, and ACF recommends this includes the Safeguard Mechanism.

The CER's role in administering the Safeguard Mechanism naturally involves close interactions with industry. Regulatory capture is a known risk that comes with established relationships between agencies and the regulated community. The separation of regulatory functions is good governance, enhances public confidence in government and helps to prevent such risks. The CCA could provide important checks and balances and improve the integrity of the Safeguard Mechanism.

#### *Recommendations*

- The CCA should complete mandatory periodic reviews of the Safeguard Mechanism (ideally every two years).
- The CCA should provide advice to the CER to inform the setting of an absolute aggregate baseline and absolute facility baselines under the Safeguard Mechanism. ACF recognises that facility-level data will inform the aggregate baseline and considers that the CER should derive absolute facility-level baselines to ensure facilities meet the 43% emissions reductions target by 2030. This is discussed further below.

### Disincentives

The consultation paper focuses on a market approach to regulation which provides incentives to good operators, including in the form of Safeguard Mechanism Credits (SMCs). SMCs provide a disincentive for poor emissions performance by requiring bad operators to purchase credits from good operators, which are likely to be competitors. This is a good start, however ACF is concerned that the operational changes needed to genuinely reduce emissions could be less attractive than running the risk and accepting the cost of current penalties and SMCs.

Penalties are currently capped at $220,000 for individuals and $2.2 million for corporations. If SMCs were worth $12 each for example (assuming one credit = one tCO2-e), it would be cheaper to take the penalty for any exceedance beyond ~185,000 tCO2e. Taking the penalty or purchasing SMCs or Australian Carbon Credit Units (ACCUs) would also be substantially cheaper than the tens or hundreds of millions required to install technology which will affect lasting deep cuts to emissions.

ACF notes that a company has never been penalised under the Safeguard, however this likely due to the flexibility afforded to date which has provided even cheaper options for dealing with potential non-

compliance. If the Safeguard is tightened and SMCs or ACCUs become scarce, disincentives will become more important. Even if non-compliance is rare, every instance will undermine the integrity of, and public confidence in, the system and could impact on industry's ability to meet targets.

Without substantial penalties to disincentivise poor performers, ACF is concerned that the Mechanism will be ineffective. A cost-benefit analysis might find that accepting a penalty is the cheapest and easiest option – this would be a perverse outcome.

*Recommendation*

- Review penalty arrangements and substantially increase penalties, including consideration of tying penalties to the magnitude of the exceedance.

## *Summary of matters where feedback is sought*

### 2. The Safeguard Mechanism's share of the national abatement task

What should the Safeguard Mechanism's share of Australia's climate targets be?

The Safeguard Mechanism should be responsible for a fair, proportional share of Australia's climate targets. In terms of the Safeguard Mechanism's share of the national abatement task, the CER's consultation paper states that "to contribute this [28%] proportional share of the national emissions target, aggregate baselines would need to fall to 99 MtCO2-e by 2030."

The multi-year emissions budget related to Australia's 2030 target results in an indicative value for the national emissions budget of "no more than 4,381 MtCO2-e for the decade from 2021 to 2030." The Safeguard Mechanism's corresponding share of the national emissions budget for the decade would be net emissions of 1,227 MtCO2-e (conservative estimate based on modelling that shows emissions covered by the Safeguard Mechanism would be expected to grow by 0.5% per year under a business-as-usual scenario).

As a further consideration, new technology is likely to show that methane emissions from the fossil fuel sector are significantly higher than currently accounted for. Any additional national emissions that are attributed to improved measurements of fossil fuel facilities will add a further emissions burden that should *not* be shared by other industries.

The legislated 43% emissions reduction target is a great start. However, for credible emissions reductions to be achieved under the Safeguard Mechanism, this target needs to ratchet up. The emissions "decline rate" under the Safeguard Mechanism needs to align with the best available science and needs to be more ambitious e.g., at least 10 Mt CO2-e per annum (or 7% of the sector's 2020–21 emissions) and not the 5 MtCO2-e per annum proposed by Reputex modelling. The Safeguard

Mechanism needs to take facilities to the 100,000 tCO2-e per annum baseline and then to net zero emissions as quickly as possible.

***Emissions reductions accounted for under the Safeguard Mechanism must reflect genuine emissions reductions, rather than annual variability in emissions.***

ACF analysis of Safeguard reported emissions data shows that, to date, aggregate emissions varied year on year by between -3.5% and +6.9%. For the Safeguard Mechanism to be effective in reducing emissions, the emissions accounted for must be reflective of absolute emissions reductions rather than annual variability. This will ensure that indicative decline rates under the Safeguard Mechanism are reflective of genuine emissions reductions and not annual variability.

To future-proof the Safeguard Mechanism, emerging technologies for measurement which might be more accurate and would increase reported emissions from facilities should be factored in. The most accurate measurement should be encouraged but should not be an excuse to increase baselines and impact the 2030 target. The Commonwealth government should analyse how much new methane measurement technology would affect total estimated emissions from Safeguard facilities, and therefore the ambition required to get to 99 MtCO2-e per annum by 2030. Additions to the abatement task that relate to improved measurement or reporting should be applied to the responsible sector rather than shared across all industries.

*Recommendations*

- The Safeguard Mechanism should be set to address its fair share of the national abatement task, currently a 28% proportional share based on reported emissions of the facilities covered, with the caveat that this proportional share should be adjusted (i.e., expanded) to account for emissions currently not counted as part of the Safeguard reported emissions due to the 100,000 tCO2-e threshold and due to inaccurate emissions measurements. Solving both problems will expand the proportional share for which Safeguard facilities are responsible.
- The Clean Energy Regulator (CER) should consider business-as-usual variability for industry when setting targets and ensure policy settings encourage material changes to operations rather than rewarding incidental emissions decreases. This is dealt with further below at: Fixed (absolute) versus production-adjusted (intensity) framework.

## 3. Setting baselines to achieve an equitable distribution of costs and benefits

### Fixed (absolute) versus production-adjusted (intensity) framework

Should we retain, and build on, the existing production-adjusted (intensity) baseline setting framework or return to a fixed (absolute) approach?

Emissions reduction needs to be the primary goal of the framework. Allowing facilities to meet targets by reducing output can have perverse outcomes, as noted in the consultation paper. On the other hand, allowing facilities to increase net emissions with increased output is just as perverse an outcome.

***A "whichever is lower" approach can ensure the primary goal of emissions reductions is achieved***

Instead of choosing a single option, ACF recommends a "whichever is lower" approach which would allow for production-adjusted baselines while ensuring that there is a ceiling on overall emissions increases.

Deep cuts need to be made and this will require material operational changes at regulated facilities. ACF is not interested in rewarding reduced emissions through reduced production (or variability discussed above) and would prefer reductions in emissions to come from genuine efficiencies and lasting change. The "whichever is lower" approach allows genuine emissions reductions to be rewarded with SMCs, and increased production (which threatens targets) to come with an additional cost.

This combination would require both emissions intensity (based on annual production) and absolute emissions (based on required reduction according to target) to be assessed each year and whichever is lower to be applied. This would ensure that it is never profitable to decrease overall emissions without also decreasing emissions intensity, and that increases in production which compromise targets necessitate a robust cost-benefit analysis.

Fixed (absolute) baselines under an ambitious Safeguard Mechanism should be *prescribed* by the CER according to emissions reduction targets and should not be adjustable based on increased production. In the first year the baseline could be fixed based on the average of historic production at a facility and industry average emissions-intensity, for example. There are many potential methods for determining the fixed baseline – the most important factor is that it is prescribed and, in subsequent years, is aligned with the reductions required by 2030.

Fixed baselines provide a ceiling for emissions, so that increased production would not allow for increased emissions – this is the only way to ensure a downward trajectory in net emissions. As mentioned earlier, the CCA should have a role in providing advice on appropriate absolute baselines.

Production-adjusted (intensity) baselines couple productivity and emissions. The Safeguard Mechanism should be first and foremost a policy to reduce emissions, not emissions-intensity. If the Mechanism exclusively concerns itself with the latter, we risk improving emissions-intensity but still seeing an increase in net emissions and failing to meet our targets. There must be some disincentive for increased production where it compromises the 2030 target.

*Recommendation*

- Use a "whichever is lower" approach to set intensity baselines at facility level plus an absolute aggregate baseline to ensure that intensity baselines do not lead to emissions increases.

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## Headroom and the need to remove it

Headroom must be removed to turn the Safeguard Mechanism into an effective policy.

As the consultation paper notes, removing headroom is crucial because:

1. Headroom is distributed unevenly across facilities;
2. If current baselines (including headroom) are retained, crediting and trading could not commence until around 2026–27; and
3. Aggregate baselines must be below aggregate emissions, or no abatement will occur.

As the consultation paper notes, "removing headroom through uniform scaling would benefit the most emissions-intensive businesses, at the expense of facilities whose emissions intensity is close to, or below, industry average. Many of these average or good performers would receive baselines that are well below their actual emissions." As such, ACF does not support uniform scaling.

While "it is proposed that the CER will automatically issue Safeguard Mechanism Credits (SMCs) to facilities with emissions below their Safeguard Mechanism baseline," any unnecessary or artificial headroom could generate SMCs that do not represent real reduction or abatement. This could undermine the basic integrity of SMCs. Although "SMCs will not need to be "additional" as defined under the *Carbon Credits (Carbon Farming Initiative) Act*", SMCs must represent real abatement that is generated by real action to reduce emissions.

The existence of headroom represents several problems, including how quickly real abatement will be achieved as baselines are reduced.

### *Recommendation*

- Reset baselines to implement the "whichever is lower approach" discussed above and remove headroom in the process.

## Setting baselines for new and existing facilities

What is the preferred approach for setting baselines for existing facilities? Approaches may include:

1. Option 1, which would see all baselines set using industry-average benchmark values.
2. Option 2, which would see all baselines set using facility-specific emissions-intensity values.
3. Other proposals, noting there are many possible approaches.

### *Industry-average benchmark values*

Option 1, with all baselines set using benchmark (industry average) emissions-intensity values appears the best option of the 2 main options considered (e.g., advantages low emissions producers, better transparency). However, this option still presents concerns. As the consultation paper observes, industry-wide benchmarks reward early adopters by creating headroom for facilities already operating more efficiently than average. This approach risks locking in headroom and reducing the incentive to further reduce emissions.

ACF recommends that all facilities are bound to baselines determined in accordance with best-practice emissions intensity values. In some industries, such as coal mining and gas supply, intensity is extremely variable across basins. This variability is reflected by the CER in, for example, the variance between the emission factor for fugitive methane in Victoria (0.0003) and NSW (0.061), and between the unaccounted-for gas pipeline factor in Tasmania (0.2) and South Australia (4.9).[7] The industry-average should therefore be set based on facilities of that class in that basin, not all facilities in that class. Ideally, the "industry average" would be based on the best-practice benchmark for each basin.

### *Facility-specific emissions-intensity values*

Facility-level emissions intensities are noted for being less transparent and not automatically rewarding the least emissions-intensive producers. This is ACF's least preferred option. If facility-level emissions intensities are set, they should be complemented with a measure to reward the least emissions-intensive producers. One way that early-adopters could be rewarded at a facility level is by giving early-adopters a bulk Safeguard Mechanism Credit for demonstrable emissions reductions. Bulk one-off crediting would reward investment in low emissions resources or technologies and past actions to reduce emissions, as well as provide a starting pool of SMCs that are robustly accounted for.

If a more accurate method is used to reset a facility's baseline, the use of that method should be locked in to 2030, so that a facility cannot start with a high baseline and then artificially create the illusion of declining emissions by reporting using a different method in future.

### *Other proposals*

Regardless of the combination of baselines applied, periodic reviews and updates will be necessary.

For example, the current 5-year average used to determine industry average emissions-intensity benchmarks is inadequate to tackle the abatement task of at least 170 MtCO2-e by 2030, and this should

[7] Commonwealth Government (2022). *National Greenhouse and Energy Reporting (Measurement) Determination 2008.* Retrieved on 17 September 2022 from: https://www.legislation.gov.au/Details/F2022C00737

be updated. In an ideal scenario, best-practice would change rapidly to 2030. Frequent updates should reflect:

- Changing science on emissions intensity factors;
- Changing accessibility of emissions-reduction technology; and
- Changing best practice in industry.

Lastly, it should be required that baselines immediately be changed to reflect care and maintenance and other operational changes. Where this has not occurred, data show that such operational changes have allowed facilities to increase their intensity and avoid accountability. For example, Glencore's Ravensworth Underground Mine reported against a baseline of 905,509 tCO2-e per annum from the 2017–21 financial years, despite having ceased operations in 2014. In 2021, the baseline was updated to 173,779 tCO2-e. If that baseline had been in effect for the 2017 and 2018 financial years, Glencore would have been required to surrender 52,093 ACCUs.

### *Setting baselines for expansions of existing facilities*

ACF notes that at least 25 current Safeguard facilities have expansion plans not currently reflected in the aggregate baseline or reported emissions, equal to an additional 218 MtCO2-e per annum run-of-mine coal. It is difficult to estimate how much these expansion plans would increase facility level emissions, since each mine uses a unique combination of calculation methods, variables and factors. However, an estimate using available records of emissions intensity puts this expansion at approximately 12 MtCO2-e per annum. Brownfields expansions pose the same risks as the new entrants identified in the consultation paper.

Scope 1 emissions can be reduced from the outset in brownfields development through design – for example, by reducing strata disturbance and using efficient haulage routes. These abatement opportunities are low-hanging fruit and, in this policy environment, best practice should be an expectation. Given this, ACF recommends that the approach applied to new entrants is also applied to brownfields expansions plans.

Without this uniformity of approach, there is a risk that operations which would otherwise be considered new facilities (such as Saraji East or Moranbah South, both categorised as new facilities in the 2021 Receiving Environment Monitoring Program (REMP) data) could be defined in reporting to the CER as expansions in order to avoid tougher standards.

In addition, expanding operations could reduce the emissions intensity across the board at a facility. Without taking a stricter approach, the Safeguard could perversely incentivise coal mines to expand. This would be dealt with by adopting the "whichever is lower" approach, coupled with a robust approach to new entrants. Further detail on ACF's recommended approach to new entrants is found in the next section.

*Recommendations*

- All facilities are bound to baselines determined in accordance with best-practice emissions intensity values.
- For fossil-fuel facilities, the industry average emissions intensity value or best-practice benchmark should be specific to each basin.
- If the government opts for facility-level emissions intensities, consider complementary measures to address concerns related to baseline-setting options.
- If a more accurate method is used to reset a facility's baseline, the use of that method should be locked in to 2030.
- Commit to periodic annual assessments of "best practice" emissions-intensity benchmarks to ensure they remain up to date.
- Require baselines to immediately be changed to reflect care and maintenance and other operational changes.
- Require the same emissions-reduction standards from brownfields expansions of existing covered facilities as for new facilities.

What are the advantages of best practice, industry average benchmarks or alternative approaches for setting baselines for new entrants?

Over time, Australia's Nationally Determined Contribution under the Paris Agreement will need to be increased, and the Safeguard Mechanism will need to keep covered facilities on a trajectory that achieves that target. We note both that the International Energy Agency found that there is no room for new oil, gas or coal to keep warming below 2 degrees and that the Safeguard Mechanism is not a lever to refuse projects.

New entrants and brownfields expansions will add to the abatement task and to aggregate covered emissions, and while the intention cannot be to stop all new entrants, these projects should be required to operate at best practice and to factor in the full cost of polluting when making their investment decisions.

New entrants and brownfields expansions have should be making investment decisions that fully incorporate climate risks and costs, including the cost of complying with the Safeguard Mechanism.

New entrants should not be given anything weaker than "best-practice" baselines. It would be reasonable to assume that "best practice" will improve rapidly so the baseline for new entrants will need to be updated over time to ensure it does not reflect outdated performance standards. At minimum, best practice should be calculated as the average emissions intensity of the top 10% of Australian industry performance.

The ideal scenario is that new entrants and brownfields expansions are required to be net zero emissions and should follow a robust avoid>minimise>mitigate>offset hierarchy that ensures efforts are centred first on design and technology, and last on carbon credits.

To underpin the integrity of the Safeguard Mechanism, the Commonwealth government should mandate the avoid>minimise>mitigate>offset hierarchy. This could be achieved placing a limit on how many ACCUs/SMCs can be used by facilities to offset emissions. The *Clean Energy Act 2011* limited the use of ACCUs to offset emissions to 5% of total emissions and this limit could be reinstated to drive actual emissions reductions. This limit could apply across all facilities covered under the Safeguard Mechanism, or just those sectors that are considered "easy to abate" and for which avoidance, minimisation and/or mitigation technology is available.

Regarding the use of site-specific intensity for new entrants, ACF agrees that this option creates an unnecessary risk of incentivising operators "to design facilities with higher emissions intensities" as well as using the highest-possible emissions calculation method, and then "reduce" emissions in a way that is artificial, thus unfairly benefiting from the scheme and artificially inflating the industry average.

*Recommendation*

- New entrants and brownfields expansions are required to be net zero emissions and should follow a robust avoid>minimise>mitigate>offset hierarchy that ensures efforts are centred first on design and technology, and last on carbon credits.

## 4. Crediting and trading, domestic offsets and international units

Are there any other issues to consider with the proposal to allow the Clean Energy Regulator to automatically issue tradable credits to Safeguard facilities whose emissions are below their baseline, with crediting and trading commencing on 1 July 2023 subject to baseline setting arrangements that remove aggregate headroom?

Should Safeguard facilities no longer be able to generate ACCUs for reducing direct (scope 1) emissions unless they have an existing registered ERF project? Further, should no new ERF projects be able to be registered at Safeguard facilities? Additional feedback is sought on:

- allowing existing ERF projects at Safeguard facilities to continue to generate credits and retaining double counting provisions to prevent a facility from generating ACCUs and SMCs;
- options for the treatment of deemed surrender;
- continuing to allow Safeguard facilities to participate in ERF projects that reduce emissions from electricity use (scope 2) emissions; and

- mechanisms to promote the transparency of the ACCU market, such as publishing unit holding, to assist with market decision making, supply and cost effectiveness.

### Safeguard Mechanism Credits (SMCs)

With the addition of SMCs, facilities should not be able to generate new ACCUs for reducing direct emissions – i.e., there should not be any new Emissions Reduction Fund (ERF) projects allowed connected to facilities that are able to generate SMCs. This is a form of double counting and an excessive return for actions long overdue from large emitters.

Any SMCs (or a category of SMCs) must be held to an integrity standard that ensures they represent real and lasting emissions reduction. SMCs should reward real action – in the form of operational changes, technological updates or other actions that indicate real, lasting emissions reduction as opposed to one-off incidental reductions and inherent variability. A system of regulating and verifying SMCs will be essential to ensure the integrity of the abatement, especially as these SMCs are traded.

#### *Case Study: A drop in emissions does not always indicate emissions-reduction activities*

While it is likely a well-reformed Safeguard mechanism will reward some of Australia's highest-emitting facilities, we must ensure that it is rewarding facilities that are making or already have made choices and investments that are impactfully bringing down emissions, rather than passively rewarding high-emitting facilities that are not acting to reduce emissions.

For example, for the 61 coal mines which reported emissions of more than 100,000 tCO2-e for the 2020–21 financial year (FY), 10 coal mines recorded a drop in emissions of more than 100,000t compared to the 2019–20 FY. From one perspective, 10 of Australia's highest-emitting facilities collectively recorded a 2.5 million tonne "drop" in reported emissions. From another perspective, they collectively caused over 7 million tonnes CO2-e of climate-heating emissions.

In this case, if we compare reported emissions to run-of-mine (RoM) coal, 7 of those 10 facilities did reduce their emissions intensity by between 13% and 66% (total scope 1 tCO2-e per tonne ROM coal). However, Safeguard data shows emissions intensity to be highly variable – in the 2019–20 FY, six out of these ten coal mines increased emissions intensity compared to the 2018–19 FY, and in the 2020–21 FY one coal mine (Grosvenor) was over 900% *more* emissions intensive (noting the mine was not operational for some of that time, but still venting fugitive methane).

It is critical that drops in emissions being rewarded by SMCs are not the result of lower production or incidental variability and are instead changes that are lasting and material.

***Prior to the introduction of production-adjusted baselines, there are several cases of significant headroom appearing in facility-level baselines due to facility operations being delayed or suspended***

Three examples:

- In the 2017–18 FY, INPEX's "Start up and Operations of the Ichthys LNG Project" went from 0 tCO2-e headroom to 6,569,849 tCO2-e headroom. This was not a consequence of emissions reductions measures, but a consequence of delayed project commencement.
- In the 2018–19 FY, Woodside's Vincent Project Venture went from 0 tCO2-e to more than half a million tCO2-e of headroom. This was because the floating production storage and offloading (FPSO) was offsite for regular maintenance for most of that financial year.
- In 2014, Glencore's Ravensworth Underground Mine ceased operations. The consequent drop in reported emissions (increase in headroom) was therefore not the result of a decision or technology intended to reduce emissions, and in fact emissions intensity increased in the sense that the mine continued to release between 150,000–200,000 tCO2-e each year.

This underscores the importance of considering production and taking the "whichever is lower" approach. SMCs should not be awarded for these forms of reduced emissions.

### Offsets

Any offsets should be from high integrity Australian projects. ACF is concerned about the integrity of ACCUs and welcomes the Chubb Review, which will also consider how Australia's domestic carbon market can provide important co-benefits if constructed well, such as greater support for biodiversity and environmental outcomes.

There are fundamental concerns with the methods issued under the ERF, leaving an abundance of inexpensive, low integrity ACCUs. ACF's investigations have uncovered that up to one in five carbon credits issued under the ERF do not represent real and additional abatement.[8] It is likely that the real figure is closer to 3 in 4 carbon credits when considering research from the ANU.[9]

ACF considers it likely the Chubb Review will recommend reform of the ERF and ACCUs, including revocation or change to methods that have been shown to produce low integrity credits. Safeguard

[8] Australian Conservation Foundation. (2022). *Serious integrity concerns around Australia's 'junk' carbon credits.* Retrieved on 17 September 2022 from: https://www.acf.org.au/integrity-concerns-around-junk-carbon-credits

[9] Andrew Macintosh, Donald Butler, Dean Ansell, Marie Waschka, Megan C. Evans, Pablo R. Larraondo and Philip Gibbons. (2022). Several pieces of research including: *Integrity Problems with the ERF's 2022 Plantation Forestry Method; Integrity and the ERF's Human-Induced Regeneration Method: The Additionality Problem Explained; Integrity and the ERF's Human-Induced Regeneration Method: The Measurement Problem Explained; Fixing the Integrity Problems with Australia's Carbon Market; The Emissions Reduction Fund (ERF): Problems and Solutions; The ERF's Human-induced Regeneration (HIR): What the Beare and Chambers Report Really Found and a Critique of its Method; Measurement Error in the Emissions Reduction Fund's Human-induced Regeneration (HIR) Method; and The Emissions Reduction Fund's Landfill Gas Method: An Assessment of its Integrity.* Retrieved on 9 September 2022 from: https://law.anu.edu.au/research/publications

facilities should be prevented from using legacy credits from methods that have been shown to be poor integrity – and the Mechanism's treatment of ACCUs should be responsive to the results of the Chubb review.

Australia cannot reach net zero emissions through offsets alone. Offsets should not be the primary means of achieving pollution reduction, and should instead sit within a hierarchy that starts with avoiding, minimising and mitigating emissions and then uses offsets as a last resort. Where technology exists to reduce emissions, the Safeguard Mechanism should incentivise its deployment. This last resort would be a stopgap until mitigation technologies and operational changes are invested in and built into business models.

As discussed above, ACF considers that the use of ACCUs should be limited to 5% of total reported annual emissions. The limit could be relaxed for hard to abate sectors; however, hard to abate and expensive to abate are not synonymous. Limits should be available to sectors with research and development challenges associated with abatement technology. If barriers to implementation are financial, for trade-exposed facilities, the Commonwealth government should consider funding technology through a co-investment model.

ACF acknowledges that offsets will play a role in the Safeguard Mechanism and Australia achieving net zero emissions. We also acknowledge that ACCUs provide important incentive and investment into the protection and regeneration of natural habitat in Australia (beyond that required by law) which is essential to ending the extinction crisis highlighted in the recent State of the Environment Report. However, the Safeguard Mechanism must be developed to ensure that offsets are not used to defer actual emissions reductions and that offsets and ACCUs have high integrity.

*Recommendations*

- Offsets should be domestic, of high integrity, and adaptive to the outcomes of the Chubb review.
- Use of offsets should be minimised to ensure that investments are made to achieve actual decarbonisation. Domestic offsets should sit within a hierarchy that starts with avoiding, minimising and mitigating emissions and then uses offsets as a last resort rather than the primary means of achieving pollution reduction.

Should international units be able to be used for compliance under the Safeguard Mechanism at a future time, noting that any decision would depend on the rules for international trading?

### International offsets

Key markets, such as the European Union Emissions Trading Scheme (EU ETS) have banned international offsets, for reasons including to prioritise domestic decarbonisation and to capture the

benefits of a low-carbon economy. The Safeguard Mechanism should avoid any use of international offsets and focus on domestic emission reduction and, where necessary, domestic offsets. International offsets are not currently required and allowing them would reduce domestic decarbonisation and undermine demand for ACCUs and associated projects.

*Recommendation*

- International Offsets should not be included in the Safeguard Mechanism. Any offsets required should be purchased from the domestic market.

Should banking and borrowing arrangements be implemented for Safeguard Mechanism Credits?

### Inter-temporal flexibility – banking and borrowing

The aim of the Safeguard Mechanism is to reduce emissions. It must be acknowledged that a tonne of CO2-e, once emitted, stays in the atmosphere and heats the planet. Maximum abatement is needed to keep global heating as close to 1.5 degrees as possible and to avoid catastrophic tipping points.

As such, timing matters just as sustained, long-term changes that reduce emissions matter. From a timing perspective, getting the most emissions reduction done early will have the greatest reward for the climate. For sustained, long-term progress there will be benefits in limiting flexibility across years. Noting the inherent variability in emissions at some facilities discussed above, ACF is concerned the banking and borrowing will allow procrastination.

The simplest version of the SMC scheme, which requires facilities to sell or buy in the earning year, essentially solves the same problem, and meets the same need. In addition, it is simpler to administer, avoids exporting risk from facilities to the aggregate baseline, and accelerates (or at least avoids deferring) the advancement of emissions-reduction technologies by incentivising operators to adopt and innovate. This incentive will not be effective if we give a free pass to operators that defer the consequences of delayed action.

Flexibility arrangements have allowed facilities to game the system and have prevented the Safeguard Mechanism from achieving its original objective of capping emissions. Access to SMCs and limited access to ACCUs provide sufficient flexibility, without eroding the integrity of the scheme.

*Recommendation*

- To ensure earlier emission reductions, remove inter-temporal flexibility arrangements, including multi-year monitoring periods. Obligations should be acquitted each year, and trading should not be allowed across years.

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## 5. Tailored treatment for emissions-intensive, trade-exposed (EITE) businesses

Should a facility-specific comparative impact assessment that builds on existing EITEs definitions be used rather than a sector wide designation?

### Defining emissions-intensive, trade-exposed facilities

A comprehensive categorisation of current Safeguard facilities would enable stakeholders to more thoroughly engage with the questions and proposals in this chapter. As the consultation paper notes, the current definition of EITE activities (as defined for the RET) would need to be adjusted before it is applied to the Safeguard facilities, but it is currently difficult to model or predict the implications of the different options proposed.

### Assistance measures for emissions-intensive, trade exposed facilities

Global efforts to decarbonise mean that the playing field for emissions intensive trade exposed (EITE) facilities has changed in recent years and will continue to change in coming years as other markets face greater climate-related requirements.

To ensure that the Safeguard Mechanism achieves genuine emissions reduction as a priority and helps Australia's industrial facilities to be as competitive as possible in a low carbon global economy, EITE facilities should not have special baselines, or special treatment within the Safeguard framework**.**

Rather than regulating EITE facilities differently, the government could provide a limited form of assistance to help with mitigation measures and achieve compliance. This could include low emissions technology funding, or access to expertise related to energy efficiency or renewable energy, **but should not include** carbon capture and storage (CCS) for fossil fuel operations.

*Recommendation*

- EITE facilities should not have special baselines or special treatment within the Safeguard framework.

Would additional funding opportunities effectively assist EITE facilities to adapt to declining Safeguard baselines?

Additional funding opportunities would effectively assist EITE facilities to adapt to declining Safeguard baselines, in some circumstances. However, EITE facilities should not be given a free ride, with funding contributing to business decarbonisation efforts, rather than covering full costs.

Emissions-reduction measures are often assessed as not economically reasonable or feasible. Providing funding tied to measurable emissions reduction solves this in two ways:

1. Providing immediate funding for immediate implementation makes already available technologies immediately accessible.
2. Higher uptake of existing technologies and higher availability of funding could lead to innovation, improvement and diversification of emission-mitigation technologies.

What kinds of funding, finance or other arrangements and measures would best support EITE Safeguard facilities to reduce their emissions?

There may be a role for the Clean Energy Finance Corporation (CEFC) to play regarding finance for mitigation solutions including new technology solutions.

Any public funding provided should be very carefully applied and tied to real, demonstrable, transparent emissions reduction. Robust and transparent accounting of reductions will be needed to ensure the reductions are real, and to accelerate the adoption and innovation of emissions reduction technologies, by allowing other facilities to see and learn from others' implementation. While it is expected that emission reduction technology will be kept a commercial secret in many cases, the Commonwealth government can and should take the opportunity to require transparency tied to use of government funds, to take advantage of the co-benefit of accelerating uptake and innovation.

Funding should only be made available where such projects are currently not economically feasible, and the operator has exhausted possible funding options. That scenario should be distinguished from a scenario in which the operator simply would prefer to access public funding, noting that some of the facilities covered under the Safeguard are posting windfall profits and should not be given taxpayer money to make their facilities less climate damaging while continuing to be extremely competitive in a global market.

*Recommendation*

- With the broader objective of the Safeguard Mechanism in mind, EITE Safeguard facilities would be best supported to reduce their emissions through access to expertise, co-investment, and funding tied to measurable emissions reductions.

In particular, what potential design features of the Powering the Regions Fund would support covered facilities with their decarbonisation priorities?

One of the priorities of the Powering the Regions Fund is to develop new clean industries. This priority is relevant to many facilities that can achieve long-term emissions reduction through fuel switching.

Another priority of the Fund is to assist existing industry to decarbonise and there is readily deployable mitigation technology, especially for fugitive methane, that facilities could embrace with the right policy settings. For example, when a price on carbon was proposed, Whitehaven reported that mitigation technology at Narrabri underground coal mine was feasible – however this was never implemented and one of the reasons given in its 2019 Independent Environmental Audit was that payback period was too long under the Emissions Reduction Fund.[10] Fugitive mitigation is no longer an innovation problem, but an engineering problem that requires site-specific solutions.

A further feature of the Fund is to assist communities that are facing transition due to coal and gas mine closures, or generator closures due to domestic and global decarbonisation efforts. Community support should be addressed through establishment of a National Energy Transition Authority, tasked with ensuring that workers and communities affected by the move to net zero emissions are supported.[11] The Authority should be funded under the Powering the Regions Fund.

*Recommendations*

- The Powering the Regions Fund could undertake feasibility studies for mitigation technology at methane-rich coal mines in the Safeguard and assist in deploying the technology with co-investment.
- Fuel switching should be a particular focus for assisting covered facilities, however this should include only genuinely useful technologies. It should not include CCS.
- Other recommended features are:
    - Only green hydrogen, no other forms.
    - No gas (either grid or captured from other facilities – unless the CER can ensure gas captured from other facilities would not be double counted as emissions reduction).
    - No fossil-fuel electricity.
    - No funding for fuel-switching that is inherently desirable based on economic benefits alone (regardless of emissions regulation).

[10] Whitehaven Coal. (2019). Independent Environmental Audit 2019. Retrieved on 15 September 2022 from: https://whitehavencoal.com.au/Documentations/Narrabri%20Mine/Environmental%20Management,%20Monitoring%20&%20Compliance/Independent%20Environmental%20Audits/NAR-Independent%20Environmental%20Audit%20Report%202019.pdf

[11] ACTU. (2022). Media Release. Retrieved on 15 September 2022 from: https://www.actu.org.au/actu-media/media-releases/2022/energy-transition-authority-critical-to-creating-secure-jobs-for-a-safer-climate#:~:text=The%20ACTU%20calls%20on%20the,ahead%20of%20the%20Jobs%20Summit.

Is the direct provision of SMCs an appropriate way to mitigate cost impacts for EITE facilities?

Direct provision of SMCs is not an appropriate way to mitigate cost impacts for EITE facilities. This would prop up an increasingly challenged industry without addressing the cause of the trade exposure challenges and without addressing the global costs of climate inaction from these facilities.

Are differential decline rates an appropriate way to reduce the impact on EITE facilities?

Differential decline rates are not the best way to assist EITE facilities, because this would reduce the near-term emissions reduction required of these facilities. As noted earlier, other forms of assistance that support investment into long-term solutions would be preferable.

How could differential decline rates be structured so that emissions reduction and fairness outcomes are maintained?

ACF considers that there is no indication this is possible.

## 6. Taking account of available and emerging technologies

Should multi-year monitoring periods be extended to allow facilities with limited near-term abatement opportunities to manage their own abatement path?

*Multi-year monitoring periods*

Multi-year monitoring periods (MYMPs) should not be extended to allow facilities with limited near-term abatement opportunities to manage their own abatement path. It is noted that "the Government understands that some facilities may face delays in accessing cost effective abatement technologies." One of the existing measures put forward through the discussion paper is multi-year monitoring periods.

ACF has strong concerns about the use of MYMPs, which reduce or delay investment in innovation by allowing operators to bet on what may emerge in the future. Operators may be compelled to wait on investment in hopes of cheaper emissions reduction technology becoming available later, leaving the cost to be worn by, and thus disadvantaging, early adopters.

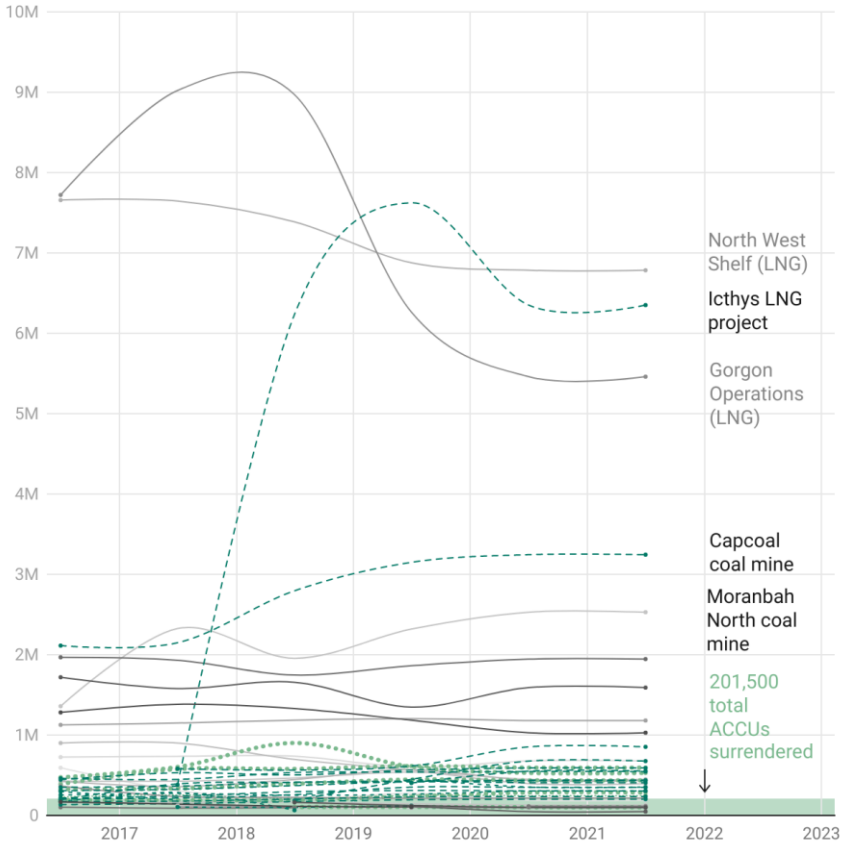
At the same time, MYMPs export risks from individual facilities to the aggregate Safeguard baseline and the Commonwealth government.

SMCs, which are likely to be introduced, offer a solution to baseline exceedance. Facilities can and should be held to their baseline each year and access the option to purchase SMCs where needed. Early adopters that invest in emissions reduction solutions and can offer SMCs will be rewarded and those that do not will pay a price that will incentivise investment in emissions reductions.

As illustrated by ACF analysis (Graph 1 below) of 53 facilities with MYMPs, 20 facilities increased their emissions after starting and MYMP (shown in red solid lines). Only 7 facilities (shown in blue dotted lines) surrendered ACCUs, and only 201,500 ACCUs were surrendered in total.

**Graph 1: Multi-year monitoring periods**

Of 53 facilities with MYMPs, 20 facilities increased* emissions (tCO2e) after starting an MYMP (shown in dashed lines). Only 7 facilities (dotted lines) surrendered ACCUs, and only 201,500 ACCUs were surrendered in total.




*Emissions are reported as tCO2e. *by at least 10%, allowing for updated emissions calculation methods*

Chart: ACF • Source: CER • Created with Datawrapper

Noting that annual baselines will not be as malleable as they were under the previous Safeguard, continuing with MYMPs still poses a risk. Chevron's Gorgon provides a useful example. Gorgon entered a MYMP because its CCS project was failing to deliver. In that period, it emitted between 8 and 9 MtCO2-e per annum. In its Environmental Impact Statement (EIS), Chevron anticipated emitting a maximum of 6.7 MtCO2-e without CCS. The additional emissions from this project alone would dramatically impact an annual ambition to reduce emissions by 5 MtCO2-e. If the next Gorgon is allowed to sail under a MYMP without a need to purchase SMCs, this could significantly undermine the Safeguard.

Companies having to pay for excessive emissions is the best way for innovation to happen quickly. We should not allow any sector to emit with impunity or delay ambition.

Should multi-year monitoring periods be extended to allow facilities with limited near-term abatement opportunities to manage their own abatement path?

MYMPs should not be extended to allow facilities with limited near-term abatement opportunities to manage their own abatement path. However, if MYMPs are made available, the two restrictions proposed in the consultation paper – ensuring that MYMPs are only available in certain circumstances and cannot under any circumstance go or be extended beyond 2030 – are essential.

Further, if the government opts to allow MYMPs, there should be a provision to deal with operators that go bankrupt or otherwise might avoid accountability for overdue SMCs incurred during a MYMP.

*Recommendation*

- MYMPs should not be available to facilities.

What are the appropriate characteristics for the decline trajectory to 2030 that can deliver the Safeguard Mechanism's share of Australia's climate targets, and the process for setting baselines post-2030?

## 7. Indicative baseline decline rates

*Recommendation*

- Avoid a "soft start" which would require a steeper decline later. This decline would be even more severe if a "soft start" were combined with high production under an intensity baseline, resulting in higher emissions.

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## 8. Other policy issues

### Role of government-defined production variables

How should landfills be treated, including:

- Should landfill baselines decline at the same rate as other facilities;
- Should landfills be able to generate SMCs in phase 1; and
- Should long-term arrangements for landfills be considered prior to phase 2?

*Recommendation*

- Landfills should not be able to access SMCs – they are already receiving an enormous amount of non-additional ACCUs under the ERF and this has led to perverse outcomes. They should decline at the same rate as other facilities.