

Submission



Emission Reduction Fund Terms of Reference

November 2013 • Contact: Erwin Jackson, Deputy CEO, ejackson@climateinstitute.org.au, 02 8239 6299

Key Recommendations

- + **Objectives:** To ensure the policy is grounded in Australia's national interest, the legislated objectives of the policy should be to help reduce Australia's carbon emissions by 5-25 per cent below 2000 levels by 2020; support the development of an effective global response to climate change, consistent with Australia's national interest in ensuring that average global temperatures increase by not more than 2°C above pre-industrial levels; and support Australia's obligations and undertakings under the UNFCCC and the Kyoto Protocol.

Recent comments by the Government have cast doubt on Australia's international commitments. The Government should clearly state to the Australian and international community if it is stepping away from the conditions for strengthening Australia's emission budgets and targets previously inscribed in numerous international agreements and declarations.

The 25 per cent reduction target represents a credible short-term contribution to our national interest goal of avoiding 2°C above pre-industrial levels. However it must also be seen as part of ongoing emissions reduction efforts that will need to be around 60 per cent below by 2030 and net zero emissions before 2050. A plan that ends in 2020 ends at the beginning.

- + **Effectiveness:** The current Emission Reduction Fund (ERF) White Paper process should involve the Productivity Commission and/or Treasury undertaking an independent analysis of emission reductions associated with proposed ERF frameworks. This should examine scenarios to expand the scope and scale of the ERF to include Government purchase of credible international emissions units to ensure Australia's international emission budget obligations are achieved and the policy can be scaled to achieve emission budgets consistent with up to 25 per cent reductions on 2000 levels by 2020.

- + **Regulatory approaches:** There is little evidence that the ERF can obtain emissions reductions consistent with even the minimum 2013-2020 carbon budgets. Substantial additional regulation is therefore required to ensure these obligations are achieved. Alongside the development of any ERF a number of important direct regulatory approaches should be maintained or implemented. These would include but are not limited to:

- *The Renewable Energy Target:* The proposed 2014 review of the RET, which TCI does not support, should clearly examine the impact of policy changes to this mechanism on the achievement of Australia's short-term and long-term emission budgets. If necessary the RET should be enhanced to ensure these goals are achieved and the electricity sector is transformed in line with the longer-term emission pathways required to meet international commitments to contribute to avoiding a 2°C increase in global temperature.
- *HFCs phasedown:* In advance of the formal agreement under the Montreal Protocol Australia should implement domestic regulations to ensure that HFC imports and use are phased down to levels consistent with the proposed amendments by the USA, Canada and Mexican proposals to this treaty.
- *Vehicle standards:* Australia should implement ambitious emissions or efficiency standards for vehicles equivalent to United States standards by 2015 and European standards by 2020.
- *Land clearing regulations:* Land-clearing laws should be re-introduced and tightened to avoid increases in emissions from this sector. The Commonwealth should play an oversight role in this regard and should exercise constitutional power to legislate should states continue to wind back these laws.

- *Energy efficiency regulations:* Important flagship policies include building codes and using the new national framework for regulating Minimum Energy Performance Standards (MEPS) to drive more ambitious equipment standards. One method would be to adapt Japan's "Top Runner" program, where continually higher performance standards are set by the most energy efficient products.
 - *Power generator standards:* Alongside or instead of emission baselines for the power sector the Government should consider setting clear regulatory standards for the power sector in line with the longer-term emission pathways required to meet international commitments to contribute to avoiding a 2°C increase in global temperature.
 - + **Credible international emission reductions:** The Government should:
 - Consider apportioning some of the ERF to credible Kyoto Protocol-compliant emission units as an insurance policy against the risk that domestically sourced abatement is not available at the scale or price required to achieve Australia's international carbon budget obligations. This insurance fund could also be used to help meet the stronger emission targets that are in our national interest.
 - Consider allowing entities captured by the mechanism applied to emissions above baseline to use credible Kyoto Protocol compliant emission units as part of the make-good process in meeting obligations.
 - + **Independent review of mechanism:** The Government has stated that it will review 2020 targets and post-2020 targets and policies in 2015. The Government needs to be flexible on this timeline as it is currently misaligned with international processes and commitments. This review should be undertaken by an independent statutory body (such as the Climate Change Authority) and must have regard to Australia's national interest in avoiding a 2°C increase in global temperature above preindustrial levels;
 - *Energy efficiency regulations:* Important flagship policies include building codes and using the new national framework for regulating Minimum Energy Performance Standards (MEPS) to drive more ambitious equipment standards. One method would be to adapt Japan's "Top Runner" program, where continually higher performance standards are set by the most energy efficient products.
 - *Power generator standards:* Alongside or instead of emission baselines for the power sector the Government should consider setting clear regulatory standards for the power sector in line with the longer-term emission pathways required to meet international commitments to contribute to avoiding a 2°C increase in global temperature.
- Australia's international obligations under international climate change agreements; undertakings relating to the reduction of carbon emissions that Australia has given under international climate change agreements; global action to reduce emissions; estimates of the global carbon budget likely to be consistent with avoiding a 2°C increase in global temperature above preindustrial levels; and an Australian carbon budget consistent with a fair contribution to this global carbon budget.
- + **Mechanism applied to emissions above baselines:** A number of key principles should apply including:
 - *Binding or voluntary:* Baselines should be binding and penalties for non-compliance should apply.
 - *Coverage:* Baselines should apply to as much of national emissions as practical. The application of emission baselines to the electricity sector will need careful consideration and should be done concurrently with the review of the RET and the development of proposed emission standards.
 - *Transparency:* The process of setting baselines and penalties should be transparent and open to independent review and challenge.
 - *Forward looking to provide long-term investment signals:* Baselines should be forward looking be set in line with current and emerging international obligations to reduce emissions.
 - *Flexibility:* Business can be given some flexibility in meeting compliance obligations under the scheme.
 - *Interaction with the ERF:* Given the challenges with establishing additionally, the Government should not fund companies for reducing emissions below their baselines under this mechanism.

Introduction

Established in late 2005, The Climate Institute (TCI) is a non-partisan, independent research organisation that works with community, business and government to catalyse and drive the change and innovation needed for a low pollution economy and culture. Our vision is for a resilient Australia prospering in a low-carbon global economy; participating fully and fairly in international climate change solutions.

This submission is structured in two parts:

- + **Overall comments and objectives.** This section addresses the key overriding issues raised by the Terms of Reference. It includes, for example, the role the Emission Reduction Fund (ERF) plays in meeting Australia's carbon budgets and international obligations.
- + **Responses to the specific issues that the Terms of Reference has raised.** This section addresses the specific question raised by the Terms of Reference with a focus on abatement options, governance arrangements and the mechanism applied to emissions above business as usual.

In framing our response to the Terms of Reference, TCI has considered its long-term emission reduction benchmarks developed in 2006. A credible domestic emission reduction strategy includes a legislated emission limit, a national price on carbon pollution, legislation to ensure all new electricity generation capacity is from zero or low emissions technologies, energy efficiency strategy to lift Australia to world class standards and a policy that allows the nation to lead efforts in the international community to deliver a global plan that avoids dangerous climate change.

We acknowledge and welcome the greater time being given to the consultations on the ERF. However, given the limited consultation period we have kept our comments largely to high level principles.

To be clear up front, TCI has deep concerns with the Government's proposed approach. No independent analysis has yet shown that the ERF and associated policies can, as they currently stand, achieve Australia's emission budgets and targets. While policies such as those proposed under the ERF can contribute to a broader emission reduction policy, there is no evidence to date that Government-funded emission reduction policies provide an effective central mechanism to deliver absolute national emission reductions on the scale required.ⁱ TCI again reiterates the risks associated with repealing a set of carbon laws that can achieve the full range of the nation's 2013-2020 emission budget and longer-term emission goals.

As outlined in our submission on the possible repeal of the current legislative package, the current system of limits, prices and incentives should remain in place until the Government can clearly demonstrate, based on independent evidence, that its proposed alternative can achieve emission budgets consistent with up to a 25 per cent reduction in emissions by 2020 and in the order of 60 per cent reductions by 2030.ⁱⁱ

Objectives of the policy

The Terms of Reference states: "The Government is committed to reducing Australia's emissions by 5 per cent from 2000 levels by the year 2020."

Australia has made a number of international commitments to contribute to avoiding dangerous climate change of greater than 2°C above preindustrial levels including to reduce emissions by up to 25 per cent on 2000 levels by 2020. The conditions for moving to stronger emission targets have been clearly outlined to the international community in a number of forums.ⁱⁱⁱ

Commitment to these goals and the conditions for stronger targets has been reiterated as Coalition policy since 2009. Recent comments by the Government have cast doubt on these commitments. The Government should clearly state to the Australian and international community whether it is stepping back from the previously articulated conditions to strengthen emission targets.

Policy credibility

The real tests of any credible emission reduction policy are: its ability to achieve the full range of Australia's emission reduction commitments and its scalability to deliver even greater emission reductions in the years after 2020.

It is clear that Australia's 5 per cent target is inadequate and the Government's agreed conditions for moving above the minimum commitment have been satisfied.^{iv} Stronger emission targets are justified not only by advances in international action and the risks to Australia from even moderate levels of climate change but also by the high economic costs and risks of delaying deeper emission cuts until after 2020.

The Climate Change Authority (CCA), for example, has noted that "A 5 per cent target would leave such large reductions for later that future Australians would either face a very large emissions reduction task or have to abandon the long term national emissions budget. This is inequitable in the first case and against Australia's national interest in the second."^v The CCA also noted that the 5 per cent target "requires an implausibly rapid acceleration of effort post 2020 to remain within the long term [carbon] budget" consistent with a 2°C goal.

Table 1: Australia's international 2020 emission commitments

International agreement	Emission Reduction Commitment
Treaties	
Doha amendments (2012): Signed but not ratified	<p>Quantified emission limitation or reduction commitment:</p> <p style="text-align: center;">0.5 per cent below 1990 levels over the period 2013-2020</p> <p>Pledged reduction in greenhouse gas emissions by 2020:</p> <p style="text-align: center;">-5 to -15 per cent or -25 per cent on 2000 levels</p> <p>Australia's target under the second commitment period of the Kyoto Protocol "is consistent with the achievement of Australia's unconditional 2020 target of 5 per cent below 2000 levels. Australia retains the option later to move up within its 2020 target of 5 to 15, or 25 per cent below 2000 levels, subject to certain conditions being met."</p>
Decisions under treaties	
Cancun Agreements (2010)	<p>"deep cuts in global greenhouse gas emissions are required ... with a view to reducing global greenhouse gas emissions so as to hold the increase in global average temperature below 2°C above preindustrial levels, and that Parties should take urgent action to meet this long-term goal"</p> <p>"Australia will reduce its greenhouse gas (GHG) emissions by 25 per cent compared with 2000 levels by 2020 if the world agrees to an ambitious global deal capable of stabilizing levels of GHGs in the atmosphere at 450 ppm carbon dioxide equivalent (CO₂ eq) or lower. Australia will unconditionally reduce its emissions by 5 per cent compared with 2000 levels by 2020 and by up to 15 per cent by 2020 if there is a global agreement which falls short of securing atmospheric stabilization at 450 ppm CO₂ eq under which major developing economies commit to substantially restraining their emissions and advanced economies take on commitments comparable to Australia's."</p>
Political commitments	
Copenhagen Accord (2009)	<p>"To achieve the ultimate objective of the Convention to stabilize greenhouse gas concentration in the atmosphere at a level that would prevent dangerous anthropogenic interference with the climate system, we shall, recognizing the scientific view that the increase in global temperature should be below 2 degrees Celsius"</p> <p>Pledged reduction in greenhouse gas emissions by 2020:</p> <p style="text-align: center;">-5 to -15 per cent or -25 per cent on 2000 levels</p> <p>"Australia will reduce its greenhouse gas (GHG) emissions by 25 per cent compared with 2000 levels by 2020 if the world agrees to an ambitious global deal capable of stabilizing levels of GHGs in the atmosphere at 450 ppm carbon dioxide equivalent (CO₂ eq) or lower. Australia will unconditionally reduce its emissions by 5 per cent compared with 2000 levels by 2020 and by up to 15 per cent by 2020 if there is a global agreement which falls short of securing atmospheric stabilization at 450 ppm CO₂ eq under which major developing economies commit to substantially restraining their emissions and advanced economies take on commitments comparable to Australia's."</p>
Majuro Declaration (2013)	<p>"Australia will unconditionally reduce its emissions by 5per cent below 2000 levels by 2020, and by up to 15per cent by 2020 if there is a global agreement which falls short of securing atmospheric stabilisation at 450 ppm carbon dioxide equivalent (CO₂-eq) under which major developing economies commit to substantially restrain emissions and advanced economies take on commitments comparable to Australia's. Australia will reduce its greenhouse gas emissions by 25per cent on 2000 levels by 2020 if the world agrees to an ambitious global deal capable of stabilising levels of greenhouse gases in the atmosphere at 450 ppm CO₂-eq or lower."</p> <p>Australia will achieve "20 per cent of electricity generation from renewables by 2020"</p>

To ensure the policy is grounded in our national interest, the legislated objectives of the policy should be:

- + take action directed towards meeting Australia's short-term target of reducing Australia's net greenhouse gas emissions by 5-25 per cent below 2000 levels by 2020
- + support the development of an effective global response to climate change, consistent with Australia's national interest in ensuring that average global temperatures increase by not more than 2°C above pre-industrial levels
- + support achievement of Australia's obligations and undertakings under the UNFCCC and the Kyoto Protocol

The current Emission Reduction Fund (ERF) White Paper process should involve the Productivity Commission and/or Treasury undertaking an independent analysis of emission reductions associated with proposed ERF frameworks. This work is also important for the preparation of an adequate Regulation Impact Statement (RIS; as per The Coalition's Policy to Boost Productivity and Reduce Regulation).

This modelling should examine scenarios to expand the scope and scale of the ERF to include Government purchase of credible international emissions units to ensure Australia's international emission budget obligations are achieved and the policy can be scaled to achieve emission budgets consistent with up to 25 per cent reductions on 2000 levels by 2020.

This modelling would also inform the required reports to the international community on progress towards achieving Australia's international commitments (e.g. under the Kyoto Protocol by end of April 2014).

Sources of low cost, large scale abatement

Australia has numerous options to reduce emissions at relatively low cost. It is unlikely that the ERF would be more efficient and effective at unlocking these opportunities than a direct carbon price. If these low cost options exist then a direct price on carbon would provide a strong incentive for investments to reduce emissions. Recent analysis for TCI by SKM MMA suggests that the current legislation will achieve around 40 per cent more domestic emission reductions than the proposed ERF.^{vi}

SKM MMA also found however that the ERF has the potential, with well-designed implementation, to achieve emission reductions in some sectors (Figure 2 and 3)^{vii}:

- + **Electricity sector:** The ERF does deliver minimal supply side emission reductions. Emission reductions in this sector mainly result from adoption of energy efficiency measures. This assumes the ERF involves deeming of energy efficiency activities. Experience from Australia's state-based energy efficiency schemes shows that unless deeming methods are

robust and regularly audited and updated they result in minimal additional emissions reduction. This increases risks that the Government would be funding activities that do not deliver emission reductions.

- + **Other stationary energy:** Some emission reductions occur from the adoption of more efficient energy practises. The level of abatement could be significantly higher in this sector if the ERF's budget constraint was relaxed because there are more energy efficient options available (at modest cost) in this sector.
- + **Transport:** Low cost emission reductions opportunities are minimal.
- + **Fugitives:** Modelled emission reductions mainly arise through flaring of methane at production facilities or coal mines, which is a relatively low cost form of abatement. Further abatement is limited by the cost of new alternative generation technologies and the increasing cost of capturing and collecting ever more quantities of methane at coal mines and gas pipes.
- + **Industrial processing:** In the modelling, emission reductions in the industrial processing sector are limited to the further replacement of cementitious material by other substitutes such as fly ash and blast furnace slag.
- + **Waste:** Emission reductions from flaring of landfill methane emissions were higher under ERF scenarios due to it being easier to account for legacy emissions as abatement.

Overall, SKM-MMA suggests that, assuming 5 to 10 year payment streams occur under the ERF at an average effective carbon pricing of around \$25/tonne to 2020, the ERF does not deliver the required levels of emission reductions required to achieve even Australia's minimum emission budget domestically.

Modelling by the Treasury for the CCA gives a similar result (Figure 4). The CCA modelling shows that abatement at the price incentives required by the budget constraints on the ERF the Government has announced (around \$5-8/tonne) would fall well short of the abatement required to achieve Australia's emission budgets. They conclude "an effective carbon price rising to over \$65/t CO₂-e by 2020 would be required to achieve the minimum 5 per cent target through domestic reductions alone."^{viii} At these prices, this would require spending \$8.5 billion in 2020 alone to achieve the minimum emission commitment.

A final point is that different abatement options require different combinations of policies to achieve outcomes. ClimateWorks, for example, has identified a range of abatement options that are better addressed through

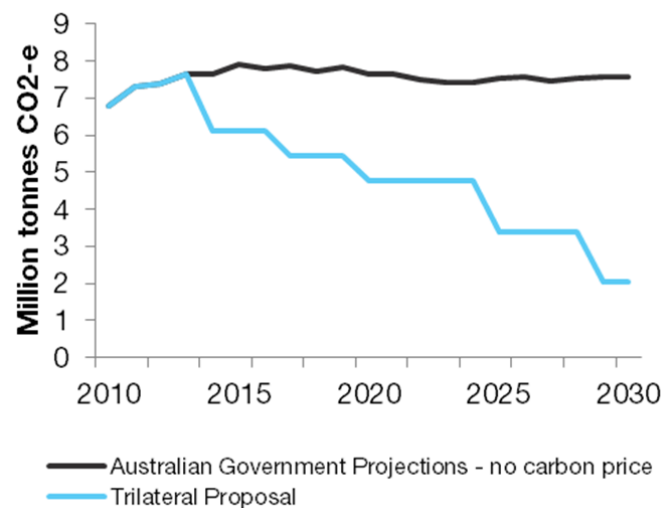
direct regulation than price signals and incentives.^{ix} Alongside the development of any ERF a number of important direct regulatory approaches should be maintained or implemented. These would include but are not limited to:

- + **Renewable Energy Target (RET):** In the absence of a legislated carbon limit and price, the Renewable Energy Target will be a central large-scale emission reduction mechanism. The Government has committed to review the RET in 2014 which will diminish its effectiveness in helping achieve Australia's emission budget to 2020. This is due to the investment uncertainty ongoing reviews create, and the resulting stalling of investment in renewable energy sources. The RET's effectiveness will be further undermined by the possible repeal of the carbon price which makes renewable energy investments more competitive^x and structural deficiencies in the electricity market.^{xi} Overall, this will make the task associated with achieving Australia's emission budgets more difficult.

The review of the RET should clearly examine the impact of policy changes to this mechanism on the achievement of Australia's short-term and long-term emission budgets. If necessary the RET should be enhanced to ensure these goals are achieved and the electricity sector is transformed in line with the longer-term emission pathways required to meet international commitments to contribute to avoiding a 2°C increase in global temperature.

- + **HFCs:** HFCs are a class of synthetic gases and are used primarily in refrigeration and air-conditioning. HFCs are powerful greenhouse gases up to thousands of times more powerful than carbon dioxide and are the fastest growing greenhouse gases in much of the world. The USA, Canada and Mexico have proposed an amendment to the Montreal Protocol that sets draft reduction targets for HFC use, whereby developed countries reduce HFCs by 85 per cent by 2033, while developing countries commit to a 40 per cent reduction by 2030. In advance of the formal agreement under the Montreal Protocol Australia should implement domestic regulations to ensure that HFC imports and use are phased down to levels consistent with the proposed amendments to the USA, Canada and Mexican proposals (Figure 1). The abatement associated with this policy would be around 15 million tonnes to 2020 and around 54 million tonnes to 2030.

compared to the impact of the USA, Canada and Mexican (Trilateral) proposal.



- + **Vehicle standards:** ClimateWorks recently concluded that strong vehicle emissions standards that have been successfully introduced or tightened in other economies could deliver substantial financial savings to Australian businesses and households and over four million tonnes of least-cost emissions reductions annually by 2020.^{xii} Australia should implement ambitious emissions or efficiency standards for vehicles equivalent to United States standards by 2015 and European standards by 2020. These standards should also set and strengthened for the period post 2020.
- + **Land-clearing regulations:** Current projections indicate that annual deforestation emissions will increase by around 25 per cent to 2020. State-based land-clearing laws have also been loosened, particularly in Queensland. The re-introduction and tightening of land-clearing regulations could avoid some or all of this increase in emissions. The Commonwealth should play an oversight role in this regard and should exercise constitutional power to legislate if states continue to wind back these laws.
- + **Energy efficiency regulations:** Energy efficiency is a key driver of energy productivity. However, Australia's approach to energy saving is patchy, and our energy efficiency is not improving at rates similar to comparable economies. Regardless of the ERF, many potential energy efficiency improvements are unlikely to be implemented, due to a range of pervasive institutional barriers.^{xiii,xiv} A range of policies are needed to make a step-change in Australian energy productivity. Important flagship policies include building codes, incentives for retrofitting existing buildings, the Energy Efficiency

Figure 1: Projected HFC emissions under current policies

Opportunities program and using the new national framework for regulating Minimum Energy Performance Standards (MEPS) to drive more ambitious equipment standards. One method would be to adapt Japan's "Top Runner"^{xv} program, where continually higher performance standards are set by the most energy efficient products.

- + **Emissions standards for generators:** A number of countries such as the USA, Canada and the UK are implementing increasingly stringent emissions standards to ensure that new and existing generators operate in line with short-term and longer-term emission constraints, and to support investment in technologies such as carbon capture and storage. Alongside or instead of emission baselines for the power sector (see below), the Government should consider setting emissions standards for the power sector as these are likely to provide clearer direction to investors and state governments on the future of fossil fuel power generation, help stimulate investment in innovative technologies such as carbon capture and storage, and act as an insurance policy to avoid the construction of new power plants that could undermine national climate change mitigation goals and/or lead to stranded assets and higher costs in future. These standards should help ensure the electricity is transformed in line with the longer-term emission pathways required to meet international commitments to contribute to avoiding a 2°C increase in global temperature.

Finally, in the original ERF policy document it was proposed that abatement purchased would have to involve other environmental benefits beyond emissions reduction; could not involve job losses; and could not lead to price rises. If applied, these conditions would add to transaction costs and significantly limit the abatement available. These conditions should not be included in further consideration of the policy.

Credible international units are a large potential source of abatement

The development of credible international carbon markets provides an opportunity to use the benefits of trade to encourage greater global ambition. The lower abatement costs provided by international markets offer an opportunity for Australia and other nations to be more ambitious in their emission-reduction commitments. Carbon markets offer the opportunity to drive substantial private sector financing in developing nations.^{xvi}

To date the Government has ruled out the use of international units in achieving the minimum nation target of 5 per cent on 2000 levels by 2020. The Government has canvassed using international units to achieve stronger emission reduction targets. To reduce the costs of achieving emission targets and ensure international obligations are met the Government should reconsider this position. Specifically, the Government should:

- Consider apportioning some of the ERF to credible Kyoto Protocol compliant emission units as an insurance policy against the risk that domestically sources abatement is not available at the scale or price required to achieve Australia's international carbon budget obligations. This insurance fund could also be used to meet the stronger emission targets that are in our national interest. Reliance on government funding of international units is not sustainable in the long term but the alternative is the possibility of Australia backsliding further on current 2020 emission commitments and undertakings. This would work against Australia's interest in securing an ambitious post-2020 climate agreement and our broader foreign policy objectives.
- Consider allowing entities captured by the mechanism applied to emissions above baseline to use credible Kyoto Protocol compliant emission units as part of the true-up process in meeting obligations (see section on mechanism above baseline emissions).

Additionality – getting value for money

The challenge with any carbon offset mechanism is establishing whether the investment that is occurring would have happened in the absence of the policy – whether it is additional. If additionality criteria are too stringent then the hurdles for investments will be too high and if the criteria are too weak the Government would be funding a project that does not deliver any additional emission reductions. The latter increases the risks that the Government will need to purchase greater amounts of emission reductions than anticipated in order to meet agreed carbon budgets and international commitments. The government will need to find a balance between these two risks. Opening the policy to international units as outlined above could be used to reduce the risk that international commitments are not achieved.

Figure 2: Modelled emission reductions by sector – Cumulative abatement 2013-2020.

Source: The Climate Institute based on SKM MMA, 2013

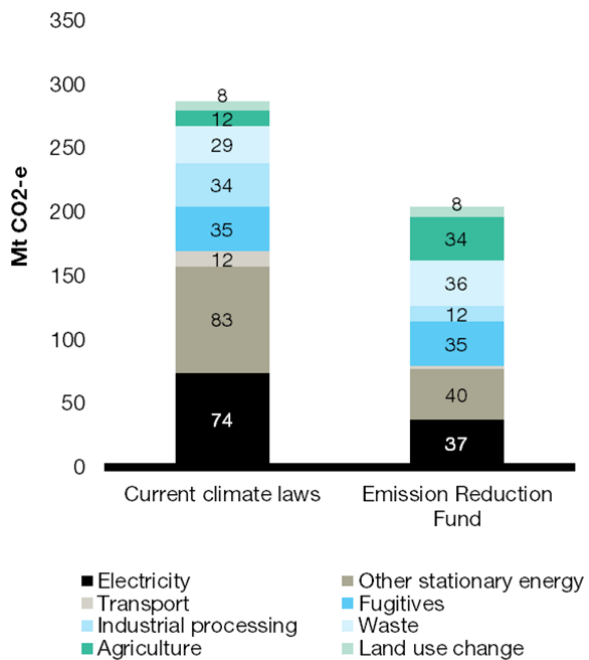


Figure 3: Proportion of emission reductions by sector under ERF – Cumulative abatement 2013-2020.

Source: The Climate Institute based on SKM MMA, 2013

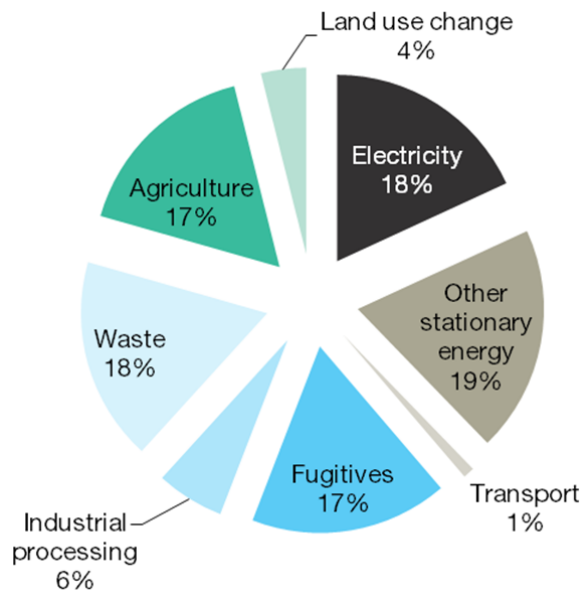
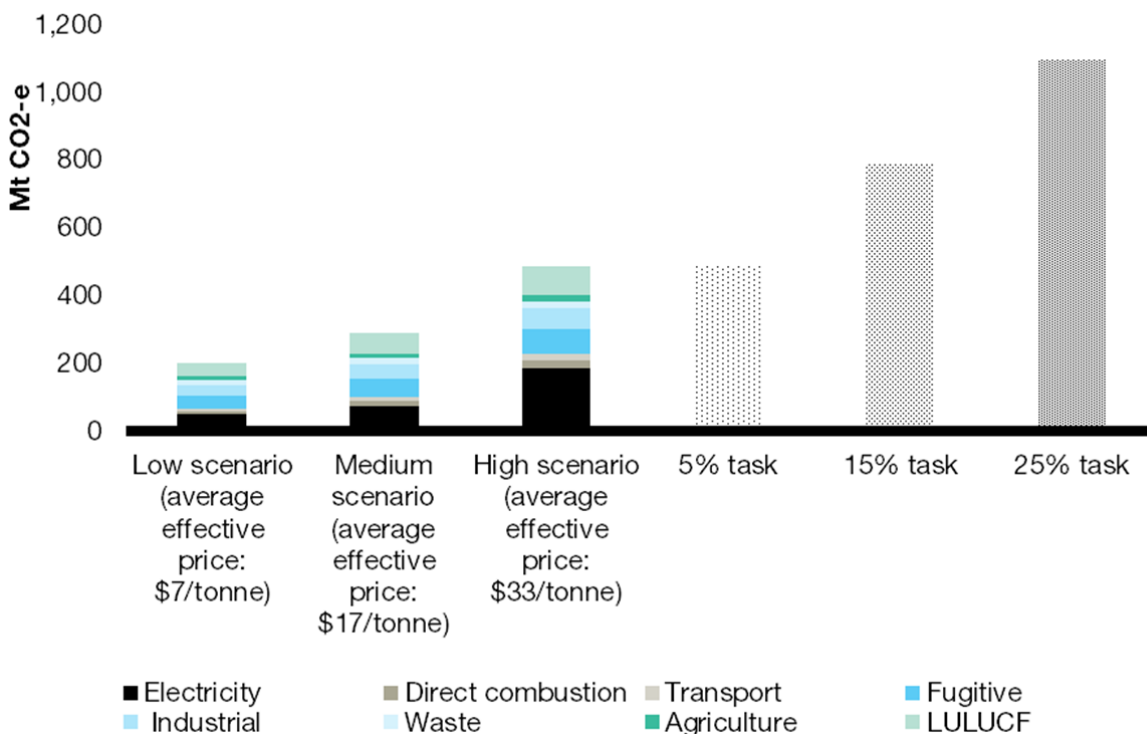


Figure 2: Cumulative modelled emission reductions under low, medium and high effective carbon price scenarios. This is compared to the emission reduction task for Australia's international commitments.

Source: The Climate Institute based on Climate Change Authority, 2013



Governance arrangements

Australia has a track record of highly politicised approaches to climate policy. This has produced policies that have often been inefficient and continually readjusted, which in turn has resulted in significant business uncertainty, higher costs associated with investments and inadequate emissions reductions.

To achieve the sustained emissions reductions consistent with its national interest, Australia needs its climate policies to be based on a sound foundation of evidence rather than a political agenda. As an independent statutory authority, the Climate Change Authority (CCA) is a cornerstone of this policy foundation. Its role as a rigorous reviewer of existing policies, along with the government's legislated requirement to respond publicly to the CCA's recommendations, ensure that the process of climate policy development and adjustment maintains a level of impartiality and transparency that would not otherwise be present if these functions were brought within a federal department.

The Productivity Commission and the Reserve Bank of Australia are clear examples of the value of ensuring that important and contentious issues are assessed by bodies independent of short-term political pressures. There is now deep and widespread support for the maintenance of these entities and their functions. The United Kingdom's Climate Change Committee, which recommends and monitors the UK's five-year carbon budgets, has been highly effective in ensuring carbon policy in the UK adheres to a sensible and stable framework.

Past Australian governments have recognised the value of ensuring independence from politics in establishing bodies such as the Productivity Commission and the Reserve Bank of Australia. Given the complexity of the climate change challenge and the politicisation of the issue, abolition of the CCA would deprive the Australian Government of an independent source of expertise, reduce the credibility of the policy development process and increase the risk that future policy decisions would be distorted by short-term political imperatives and interest groups.

As TCI have outlined in our submission to the potential repeal of the Clean Energy Future Act, to help ensure key policy decisions are not arbitrarily made and to preserve community and business confidence in the independence, impartiality and transparency of climate policy reviews the government should not abolish the CCA. The CCA must be maintained in its current form, with responsibility for reviewing key federal climate policies.

An independent 2015 review

The Government has stated that it will review 2020 targets and post 2020 targets and policies in 2015. The Government needs to be flexible on this timeline it currently appears misaligned with international processes and commitments.

In the absence of the Climate Change Authority undertaking this review the Government should clarify the parameters of this review in the ERF process.

This review must have regard to:

- Australia's national interest in avoiding a 2°C increase in global temperature above preindustrial levels
- Australia's international obligations under international climate change agreements
- undertakings relating to the reduction of carbon emissions that Australia has given under international climate change agreements
- global action to reduce carbon emissions
- estimates of the global carbon budget likely to be consistent with avoiding a 2°C increase in global temperature above preindustrial levels
- an Australian carbon budget consistent with a fair contribution to the global carbon budget likely to be consistent avoiding a 2°C increase in global temperature above preindustrial levels

The report of the review must be published as soon as practicable after being given to the Government. If the report sets out one or more recommendations to the Government must prepare a statement setting out its response to each of the recommendations and within 6 months after receiving the report, the table this statement in each House of the Parliament.

Mechanism applying to emissions above the business as usual baseline

There are very many possible permutations of how baselines could be applied: facility versus corporate group, intensity versus absolute, and historical versus forward-looking are just some of the firm policy decisions that will need to be made. Within these various elements there are also different approaches within different sectors could be undertaken, for example, intensity baselines based on production, revenue and/or value add.

There are also issues as to whether firms breaching their baseline could potentially have alternatives to paying a penalty, e.g. purchases of emissions units Carbon Farming Initiative offsets and/or international options.

In defining the broad macro policy settings for the mechanism applied to emissions above baselines a number of key principles should apply:

- + **Binding or voluntary:** Baselines should be binding and penalties for non-compliance should apply. Voluntary baselines would be a compliance burden on industry with no benefit.

- + **Coverage:** Baselines should apply to as much of national emissions as practical. The application of emission baselines to the electricity sector will however need careful consideration and should be done concurrently with the review of the RET and the development of TCIs proposed emission standards.

The original Direct Action Plan states that “Provision will be made to ensure penalties will not apply to new entrants or business expansion at ‘best practice.’” If baselines apply to the electricity sector, at a minimum, the best practice standard for coal plants should 200 kgCO₂-e/MWh and non-peaking gas must be built with the demonstrated ability to retrofit to this same standard 15 years after construction.

- + **Transparency:** The process of setting baselines and penalties should be transparent and open to independent review and challenge.

- + **Forward looking to provide long-term investment signals:** Baselines should be forward looking be set in line with current and emerging international obligations to reduce emissions.

- + **Flexibility:** Business can be given some flexibility in meeting compliance obligations under the scheme. If a company exceeds the baseline a make good option should apply. Specifically, the make good option would include submitting credible Kyoto Protocol compliant emission units (international or through the Carbon Farming Initiative) to meet obligations.

- + **Interaction with the ERF:** Given the challenges with establishing additionally, the Government should not fund companies for reducing emissions below their baselines under this mechanism. Government funds should be focused on quality emission reductions that can clearly contribute to meeting Australia international emission obligations. Using Government funds increases the risk that Australia will not comply with international commitments increasing fiscal risks.

ENDNOTES

- ⁱ The Climate Institute, 2013a, *Coalition Climate Policy and the National Climate Interest*, TCI, Sydney.
- ⁱⁱ O. Kember, E. Jackson with M. Chandra, 2013, *GHG Mitigation in Australia: An Overview of the Current Policy Landscape*, Working Paper, World Resources Institute, Washington, DC.
- ⁱⁱⁱ For example see Australian Government submission to the Kyoto Protocol, 2012:
<http://www.climatechange.gov.au/sites/climatechange/files/files/australia-qelro-submission.pdf>
- ^{iv} For example, The Climate Institute, 2013b, *Submission to the Climate Change Authority Caps and Targets Review*, TCI, Sydney.
- ^v Climate Change Authority, 2013, *Reducing Australia’s Greenhouse Gas Emissions: Targets and Progress Review Draft Report*, CCA, Melbourne.
- ^{vi} The Climate Institute, 2013, *ibid.*
- ^{vii} Note for the agriculture sector, abatement mainly comes from improved soil management practises. For the reference case, abatement was obtained from projections from the government. It was assumed that abatement was greater in the base policy cases due to the expansion of options around soil carbon restoration as eligible abatement measures.
- ^{viii} Climate Change Authority, 2013, *ibid.*
- ^{ix} ClimateWorks Australia, 2013a, *Tracking Progress Towards a Low Carbon Economy*, ClimateWorks Australia, Melbourne.
- ^x The Climate Institute, 2013a, *ibid.*
- ^{xi} See T. Nelson, 2013, *Investment in new generation in the NEM*, <http://www.aglblog.com.au/wp-content/uploads/2013/10/TN-Presentation.pdf>
- ^{xii} ClimateWorks Australia, 2013, personal communication.
- ^{xiii} For example in industrial sector, ClimateWorks Australia, 2013b, *Industrial Energy Efficiency Data Analysis Project: Draft detailed results for comment*, Executive Summary, ClimateWorks Australia and Department of Resources, Energy and Tourism, May 2013.
- ^{xiv} For example in building sector, ClimateWorks Australia, 2010, *Australian Carbon Trust Report: Commercial buildings emissions reduction opportunities*, ClimateWorks Australia; ClimateWorks Australia, 2011, *Low Carbon Growth Plan for Australia: Retail Sector Summary Report*, ClimateWorks Australia.
- ^{xv} In Japan, their flagship energy efficiency Top Runner program has been in operation since 1998. Top Runner standards are set to ensure the average efficiency of the rest of the market meets the performance level of most efficient products available (generally within three years). The standards have been revised and expanded, and now cover 21 types of products ranging from vehicles to electric rice cookers. To date, the program has seen energy efficiency improvements of between 16–80 per cent across the products covered.
- ^{xvi} High-level Advisory Group on Climate Change Financing, 2010.