

The Senate

Environment and Communications
Legislation Committee

Carbon Farming Initiative Amendment Bill
2014 [Provisions]

July 2014

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Committee membership

Committee members to 30 June 2014

| | |
|-------------------------------------|------------------------|
| Senator John Williams, Chair | NATS, New South Wales |
| Senator Anne Urquhart, Deputy Chair | ALP, Tasmania |
| Senator David Fawcett | LP, South Australia |
| Senator Louise Pratt | ALP, Western Australia |
| Senator Anne Ruston | LP, South Australia |
| Senator Larissa Waters | AG, Queensland |

Committee members from 1 July 2014

| | |
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| Senator Anne Urquhart, Deputy Chair | ALP, Tasmania |
| Senator Matthew Canavan | NATS, Queensland |
| Senator James McGrath | LP, Queensland |
| Senator the Hon Lisa Singh | ALP, Tasmania |
| Senator Larissa Waters | AG, Queensland |

Substitute members

Senator Christine Milne (AG, Tasmania) to replace Senator Larissa Waters (AG, Queensland) for this inquiry

Senator Anne McEwen (ALP, South Australia) to replace Senator Anne Urquhart (ALP, Tasmania) on 1 July 2014

Participating members

Senator Nick Xenophon (IND, South Australia)

Committee secretariat

Ms Christine McDonald, Committee Secretary
Ms Sophie Power, Principal Research Officer
Ms Meryl Hampson, Research Officer
Mrs Dianne Warhurst, Administration Officer

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Chapter 1

Background

Introduction

1.1 On 19 June 2014, on the recommendation of the Senate Selection of Bills Committee, the Senate referred the provisions of the Carbon Farming Initiative Amendment Bill 2014 (the bill) to the Senate Environment and Communications Legislation Committee (the committee) for inquiry and report by 7 July.¹

1.2 The Selection of Bills Committee set out the following as reasons for referral and principal issues for consideration:

- the impact and operation of the Carbon Farming Initiative amendments on existing land sector projects and changes to research and development;
- the application of the Carbon Farming Initiative to other industry areas and community energy efficiency projects; and
- the role and operations of Australian Carbon Credit Units in a grant-based system.²

Conduct of the inquiry

1.3 In accordance with the usual practice, the committee advertised the inquiry on its website and invited relevant organisations to make submissions by 26 June 2014.³

1.4 The committee received 17 submissions relating to the bill. These are listed at Appendix 1 and may be accessed through the committee's website.

1.5 The committee held a public hearing in Canberra on 1 July 2014. A list of witnesses who appeared at the hearing may be found at Appendix 2.

1.6 The committee thanks all the organisations and individuals that contributed to the inquiry and the witnesses who participated in the public hearing.

Notes on references

1.7 Hansard references in this report are to the proof committee Hansard. Page numbers may vary between the proof and the official Hansard transcript.

1 *Journals of the Senate*, No. 33, 19 June 2014, pp 914–916.

2 Senate Selection of Bills Committee, *Report No. 7 of 2014*, Appendix 4.

3 Senate Standing Committee on Environment and Communications website, 'Carbon Farming Initiative Amendment Bill 2014 [Provisions]', http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Environment_and_Communications (accessed 23 June 2014).

Purpose of the bill

1.8 The purpose of the bill is to provide the framework to administer the Emissions Reduction Fund, the establishment of which is a Coalition election commitment. The Emissions Reduction Fund is a significant element of the Government's policy to respond to climate change.⁴

1.9 The legislation proposes to extend the reach of the Carbon Farming Initiative to allow for the crediting of emissions reduction projects across more sectors of the economy. It proposes to broaden the powers of the Clean Energy Regulator to purchase emissions reductions and streamlines existing processes under the Carbon Farming Initiative.⁵

1.10 The bill principally amends the *Carbon Credits (Carbon Farming Initiative) Act 2011* and makes minor amendments to the *National Greenhouse and Energy Reporting Act 2007*, the *Australian National Registry of Emissions Act 2011* and the *Clean Energy Regulator Act 2011*.⁶

1.11 The Minister for the Environment, the Hon Greg Hunt, in his second reading speech concluded:

By building on the success of the Carbon Farming Initiative, this Bill supports positive action by farmers, businesses and households.

This Bill will use positive incentives to reduce emissions, unlock economic benefits, boost energy efficiency and improve agricultural productivity...This Bill will deliver these results through the Emissions Reduction Fund.⁷

Background to the bill

1.12 At the 2013 federal election, the Coalition committed to the repeal of the carbon price and the implementation of its Direct Action Plan on climate change and carbon emissions.⁸ The Emissions Reduction Fund is a key element of the Direct Action Plan. It is designed to support activities that reduce greenhouse gas emissions and to contribute to Australia meeting its emissions reduction target under the Kyoto

4 The Hon Greg Hunt MP, Minister for the Environment, *House of Representatives Hansard*, 18 June 2014, p. 9.

5 The Hon Greg Hunt MP, Minister for the Environment, *House of Representatives Hansard*, 18 June 2014, pp 10–11.

6 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 8.

7 The Hon Greg Hunt MP, Minister for the Environment, *House of Representatives Hansard*, 18 June 2014, p. 13.

8 The Coalition, *The Coalition's policy to scrap the carbon tax and reduce the cost of living*, <http://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query%3DId%3A%22library%2Fparty%2F2645370%22> (accessed 24 June 2014).

Protocol.⁹ The bill implements the Emissions Reduction Fund, which is based on three key principles:

- to encourage projects that deliver lowest cost emissions reductions;
- emissions reductions will be genuine and go beyond 'business-as-usual'; and
- streamlined and cost-effective administration.¹⁰

Consultation process

1.13 Prior to the introduction of the bill, the Government undertook a consultation process.¹¹ In October 2013, the Government invited submissions on its terms of reference for the Emissions Reduction Fund. More than 290 submissions were received in response to the terms of reference. The subsequent Green Paper, released in December 2013, outlined options for the design of the fund, and invited submissions by 21 February 2014. More than 340 submissions were received in relation to the Green Paper.¹²

1.14 The design of the Emissions Reduction Fund was also guided by an Expert Reference Group, comprising leading industry and academic experts, appointed for their knowledge of, and expertise in, the sector. The scope of the group's advice was determined by the terms of reference for the Emissions Reduction Fund. According to the Department of the Environment, the Expert Reference Group has met a number of times and 'will be convened as required to provide advice on aspects of the Emissions Reduction Fund that have yet to be finalised, such as the safeguard mechanism'.¹³

White Paper

1.15 The final design of the Emissions Reduction Fund was outlined in the White Paper that was issued on 24 April 2014.¹⁴ In the White Paper, the co-chairs of the Expert Reference Group stated that there was 'broad agreement on a number of key

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- 9 The Coalition, *The Coalition's direct action plan: environment and climate change*, <http://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;adv=yes;orderBy=customrank;page=0;query=%22direct%20action%22%20Dataset%3Apartyol;rec=1;resCount=Default> (accessed 24 June 2014); Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 11.
- 10 The Hon Greg Hunt MP, Minister for the Environment, *House of Representatives Hansard*, 18 June 2014, p. 10.
- 11 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, pp 9–10.
- 12 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 9; Department of the Environment, *Emissions Reduction Fund*, <http://www.environment.gov.au/climate-change/emissions-reduction-fund> (accessed 24 June 2014).
- 13 See further Department of the Environment, *Expert Reference Group on the design of the Emissions Reduction Fund*, <http://www.environment.gov.au/climate-change/emissions-reduction-fund/expert-reference-group> (accessed 26 June 2014).
- 14 Australian Government, *Emissions Reduction Fund White Paper*, April 2014, <http://www.environment.gov.au/climate-change/publications/emissions-reduction-fund-white-paper> (accessed 26 June 2014).

policy settings to ensure the Emissions Reduction Fund made an effective contribution to reducing greenhouse gases in Australia'. Those key policy settings include:

- the need for an effective safeguard mechanism;
- the operation of baselines that permit sustainable economic growth;
- ensuring the Government only sponsors projects that would not otherwise proceed but would make a genuine contribution to achieving the targeted reduction in greenhouse gases;
- ensuring there is no net increase in the administrative burden on industry;
- ensuring the commercial arrangements associated with the operation of the Emissions Reduction Fund attract economic investments;
- reducing duplication and overlaps between Commonwealth and state policies to reduce greenhouse gases;
- to the extent possible, develop the Emissions Reduction Fund in a way that can mesh in with a range of international initiatives to reduce greenhouse gases; and
- recognition of the important role of local communities in achieving sustainable outcomes.¹⁵

1.16 The White Paper noted that the 'overriding objective of the Emissions Reduction Fund will be to reduce emissions at lowest cost over the period to 2020, and make a contribution towards Australia's 2020 emissions reduction target of five per cent below 2000 levels by 2020'.¹⁶

Exposure draft legislation

1.17 On 9 May 2014, the Government released the Emissions Reduction Fund exposure draft legislation and explanatory memorandum for public consultation. The consultation period closed on 23 May 2014.¹⁷ The Department of the Environment published a document detailing the results of the consultation on the draft legislation on 18 June 2014.¹⁸

Relevant existing programs and entities

1.18 It is proposed that some existing programs and entities will be retained in the implementation of the Emissions Reduction Fund under the bill. In particular:

15 Australian Government, *Emissions Reduction Fund White Paper*, April 2014, p. 4.

16 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 10.

17 Department of the Environment, *Emissions Reduction Fund – Legislation*, <http://www.environment.gov.au/climate-change/emissions-reduction-fund/legislation> (accessed 26 June 2014).

18 Department of the Environment, *The Emissions Reduction Fund: The Results of Consultation on Draft Legislation*, 18 June 2014, <http://www.environment.gov.au/system/files/pages/7aef9f12-8ba1-4d9a-bf6a-1bc89a0bd6f5/files/erf-exposure-draft-legislation-consultation.pdf> (accessed 26 June 2014).

- key elements of the Carbon Farming Initiative will be retained and incorporated into the Emissions Reduction Fund; and
- the Clean Energy Regulator will administer the scheme.¹⁹

1.19 A brief outline of each of these existing schemes is set out below.

Carbon Farming Initiative

1.20 The Carbon Farming Initiative is a voluntary scheme established with the purpose of creating incentives for carbon abatement or avoidance projects in land use sectors. The Carbon Farming Initiative operates under the *Carbon Credits (Carbon Farming Initiative) Act 2011* (CFI Act) and is administered by the Clean Energy Regulator. It is currently targeted at landholders who can undertake eligible offset projects and earn carbon credits.²⁰

1.21 The Carbon Farming Initiative enables individuals and entities to earn Australian carbon credit units (ACCUs) through activities that store carbon or reduce greenhouse gas emissions on the land. Each ACCU represents one tonne of carbon emissions abatement. ACCUs earned under the Carbon Farming Initiative can be sold to people and businesses wishing to offset liability under the carbon pricing mechanism, or to voluntarily offset their emissions.²¹

1.22 Methodology determinations set out the rules for undertaking activities under the Carbon Farming Initiative which earn ACCUs. The methodology determinations explain how to carry out an abatement project and measure the resulting reductions in greenhouse gas emissions. There are two primary types of methodology determinations: sequestration and emissions avoidance.²²

1.23 The Domestic Offsets Integrity Committee is an independent expert group currently tasked with assessing methodologies and advising the minister. The minister decides whether to make methodology determinations, which must be based on methodology proposals that have been endorsed by the Domestic Offsets Integrity Committee.²³

19 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, pp 6–7.

20 Department of the Environment, *Carbon Farming Initiative*, <http://www.climatechange.gov.au/reducing-carbon/carbon-farming-initiative> (accessed 26 June 2014).

21 Clean Energy Regulator, *Carbon Farming Initiative*, <http://www.cleanenergyregulator.gov.au/Carbon-Farming-Initiative/Pages/default.aspx> (accessed 26 June 2014).

22 Note that sequestration projects generate abatement by removing carbon dioxide from the atmosphere and storing it as carbon in plants as they grow. Emissions avoidance projects generate abatement by reducing or avoiding emissions. Clean Energy Regulator, *Methodology determinations*, <http://www.cleanenergyregulator.gov.au/Carbon-Farming-Initiative/methodology-determinations/Pages/default.aspx> (accessed 26 June 2014).

23 Department of the Environment, *Domestic Offset Integrity Committee*, <http://www.climatechange.gov.au/reducing-carbon/carbon-farming-initiative/domestic-offsets-integrity-committee> (accessed 26 June 2014).

1.24 The Carbon Farming Initiative presently covers projects that occur in the agriculture and land use sectors, as well as projects to reduce emissions from legacy landfill waste.²⁴ There are currently 22 methodology determinations. Some of the approved methodologies under the Carbon Farming Initiative include:

- reduction of emissions from the waste sector;
- management of savanna burning in the Northern Territory; and
- capture of methane generated from manure at a piggery.²⁵

1.25 The CFI Act requires the Clean Energy Regulator to publish and maintain a web-based Register of Offsets Projects, which includes the number of ACCUs issued. At 26 June 2014, 135 eligible offsets projects had been registered.²⁶

1.26 To be eligible for ACCUs under the Carbon Farming Initiative, projects must deliver extra reductions in greenhouse gas emissions—that is, reductions that are additional to what would have occurred in the absence of the project. This is known as 'additionality'.²⁷

1.27 Under the Carbon Farming Initiative, projects are also subject to a permanence obligation, meaning that carbon stores must be maintained for at least 100 years. This is known as 'permanence'.²⁸

Clean Energy Regulator

1.28 The Clean Energy Regulator is established by the *Clean Energy Regulator Act 2011* (Cth) and is responsible for administering the carbon pricing mechanism, the National Greenhouse and Energy Reporting Scheme (NGERS), the Renewable Energy Target and the Carbon Farming Initiative. The Clean Energy Regulator's current responsibilities also include functions relating to the carbon pricing mechanism.²⁹

24 Department of the Environment, *Activities – eligible and excluded*, <http://www.climatechange.gov.au/reducing-carbon/carbon-farming-initiative/activities-eligible-and-excluded#scope> (accessed 26 June 2014).

25 Department of the Environment, *Methodology determinations*, <http://www.climatechange.gov.au/reducing-carbon/carbon-farming-initiative/methodologies/methodology-determinations> (accessed 26 June 2014).

26 Clean Energy Regulator, *Register of Offsets Projects*, <http://www.cleanenergyregulator.gov.au/Carbon-Farming-Initiative/Register-of-Offsets-Projects/Pages/default.aspx> (accessed 26 June 2014).

27 The additionality test is currently set out in section 41 of the CFI Act. See also Department of the Environment, *About the CFI*, <http://www.climatechange.gov.au/reducing-carbon/carbon-farming-initiative/about-cfi> (accessed 2 July 2014).

28 Department of the Environment, *Permanence*, <http://www.climatechange.gov.au/reducing-carbon/carbon-farming-initiative/activities-eligible-and-excluded/permanence> (accessed 26 June 2014).

29 Clean Energy Regulator, *Our work*, <http://www.cleanenergyregulator.gov.au/About-us/our-work/Pages/default.aspx> (accessed 26 June 2014).

Chapter 2

Overview of the bill

2.1 This chapter provides an overview of key aspects of the bill.

Introduction

2.2 The Carbon Farming Initiative Amendment Bill 2014 (the bill) amends the *Carbon Credits (Carbon Farming Initiative) Act 2011* (the CFI Act) and makes minor amendments to related Acts¹ to allow for the establishment of the Emissions Reduction Fund. Specifically, the bill proposes to amend the CFI Act to 'implement the crediting and purchasing components of the Emissions Reduction Fund'.² The bill also proposes to expand the Carbon Farming Initiative to make it accessible to emissions reduction activities across the economy, not just land-based projects. It proposes to empower the Clean Energy Regulator (the Regulator) to hold auctions, enter into contracts and buy emissions reductions. The bill also proposes to streamline current processes and provide for the transition of existing participants under the Carbon Farming Initiative.

Emissions Reduction Fund

2.3 According to the Explanatory Memorandum, the Emissions Reduction Fund will commence operations following the repeal of the carbon tax.³ The 2014–15 budget allocation for the fund is \$2.55 billion.⁴ The Clean Energy Regulator will be able to 'commit under contract the full level of funding from the commencement of the Fund'.⁵

2.4 The three elements of the Emissions Reduction Fund are:

- credit emissions reductions;
- purchase emissions reductions; and
- safeguard emissions reductions.⁶

Crediting emissions reductions

2.5 The bill empowers the Clean Energy Regulator to allocate Australian carbon credit units (ACCUs) to eligible carbon abatement projects across a broader range

1 Specifically, the *National Greenhouse and Energy Reporting Act 2007*, the *Australian National Registry of Emissions Act 2011* and the *Clean Energy Regulator Act 2011*.

2 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 11.

3 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 5. Note, however, that the commencement provisions of the bill do not appear to be contingent upon the repeal of the carbon tax legislation.

4 See *Committee Hansard*, 1 July 2014, p. 17.

5 Australian Government, *Budget Paper No. 2 2014–15*, pp 102–103.

6 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 6.

than under the existing legislation. The bill proposes to expand the types of projects able to be credited under the Carbon Farming Initiative to any type of project to avoid greenhouse gas emissions, not just land-based projects and certain types of waste projects.⁷

2.6 As it does under the current legislation, the Regulator will issue ACCUs to registered projects for each tonne of carbon dioxide equivalent reduced or stored in the land. ACCUs will be issued once emissions reductions have been estimated using approved methodologies, and, where necessary, independently audited. A project will need to be registered before it can participate in an Emissions Reduction Fund auction or other purchasing process.⁸

Developing methodologies

2.7 As outlined in the previous chapter, the Carbon Farming Initiative uses methodologies to estimate emissions reductions across activities. The bill intends to change the way methodologies are proposed, assessed and made under the Emissions Reduction Fund.⁹

2.8 Under the current framework, methodologies can be proposed by anyone, and a minimum period of 40 days of public consultation follows. The Minister for the Environment can only make a methodology if it has been endorsed by the Domestic Offsets Integrity Committee and complies with, among other requirements, the offsets integrity standards. The offsets integrity standards currently require that emissions reductions be 'measurable, capable of being audited, and estimated on the basis of conservative assumptions'.¹⁰ The offsets integrity standards requirements will remain under the regime proposed by the bill.

2.9 Under the Emissions Reduction Fund the Minister for the Environment would identify priorities for methodology development, following consultation with technical working groups and advice from the renamed 'Emissions Reduction Assurance Committee'.¹¹ The process for anyone to propose methodologies will be repealed¹² and the 40-day consultation period reduced to 28 days.¹³

2.10 The Explanatory Memorandum states that this streamlined process:

7 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 24. See also item 143 of Schedule 1 of the bill.

8 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, pp 21 and 55; item 5 of Schedule 1 of the bill.

9 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 35 and see comparison of key changes at pp 36–38.

10 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 42.

11 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, pp 35 and 45.

12 Carbon Farming Initiative Amendment Bill 2014, Schedule 1, items 205, 207, 209 and 211.

13 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 36 and Schedule 1, items 204 and 123A–D.

...will focus methodology development on opportunities that generate the largest volume of genuine abatement and that are likely to encourage the most participation.¹⁴

Crediting periods

2.11 Under the Carbon Farming Initiative, projects are approved and registered for a specified 'crediting period', which is the period during which emissions reduction activities are eligible to generate credits.¹⁵ Currently, the standard crediting period is seven years unless a different crediting period is specified through the regulations. The bill proposes a standard seven-year crediting period for emissions reductions projects and 25 years for sequestration projects. The bill also enables different lengths of crediting period to be provided through methodologies.¹⁶

2.12 The White Paper explained that flexibility is provided by allowing crediting periods of different durations depending on the project:

...methods can also provide for shorter, three-year crediting periods or longer, 10-year crediting periods in certain circumstances. This recognises that some activities are likely to remain additional to business as usual for significantly shorter or longer periods than the standard seven-year crediting period.

For example, while a seven year crediting period would be provided for a whole-of-building energy efficiency upgrade, a shorter crediting period could be considered for some space heating projects that are likely to become business as usual very quickly.

Conversely, large and ambitious projects with the potential to make a substantial single contribution towards reducing Australia's emissions may require longer crediting periods. These projects could be provided with a 10-year crediting period...¹⁷

2.13 Currently, after the first crediting period has expired, project proponents can apply for a subsequent crediting period. The bill proposes to remove the ability for projects to have more than one crediting period.¹⁸ The Explanatory Memorandum states that this will 'ensure that the Emissions Reduction Fund continues to target new projects that build on previous gains'.¹⁹

Additionality

2.14 To be eligible to receive credits under the current legislation, a project must undergo an 'additionality' test. The Explanatory Memorandum defines 'additionality'

14 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 35.

15 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 32.

16 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 32.

17 Australian Government, *Emissions Reduction Fund White Paper*, April 2014, p. 33.

18 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 33 and Schedule 1, item 152.

19 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 33.

as a requirement that a project or activity produce emissions reductions that are most likely to be additional to what would have occurred in the absence of the Emissions Reduction Fund. The current test requires a project to go beyond common practice and be listed on the 'positive list' under the CFI Regulations. The project must also not be required by another law. The bill proposes to repeal the existing additionality 'common practice' test and the associated separate 'positive list' process. It will be replaced with new project eligibility requirements and an express definition of additionality in the offsets integrity standards, which require that a methodology must result in carbon abatement that is unlikely to occur in the ordinary course of events.²⁰ The concept of 'common practice' remains a useful way to determine whether an activity is additional and is likely to be incorporated in the context of methodology development and assessment.²¹

2.15 Under the proposed project eligibility requirements, the bill introduces a new requirement that projects likely to occur because of funding from another Commonwealth or state government program will not be eligible to receive support from the Emissions Reduction Fund. This does not preclude projects from receiving other types of funding or support:

It is not the Government's intention to prevent proponents from obtaining funding or in-kind support from multiple sources where this is necessary for the project. For example, the Government anticipates that environmental projects could receive assistance from the Green Army and fire management projects may involve rangers involved in Indigenous ranger programmes.²²

Purchasing emissions reductions

2.16 The bill authorises the Clean Energy Regulator to buy emissions reductions on behalf of the Commonwealth. The ability to purchase emissions reductions, enter into contracts and enforce contract provisions is a new responsibility for the Regulator. Purchasing will generally be done through reverse auctions to obtain emissions reductions at the lowest cost, although the Regulator will also have discretion to purchase emissions reductions through other processes such as tendering.²³ As noted earlier, a project must be registered in order to be included in an auction or other purchasing process.

2.17 The Regulator will design the purchasing process:

The Regulator's discretion will be bound by principles outlined in the legislation. The principles require the Regulator to, among other matters, design the purchasing process to deliver value for money, maximise

20 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, pp 30, 42 and Schedule 1, items 25, 107 and 223 of the bill.

21 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 30.

22 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 31.

23 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 53.

abatement, minimise administrative costs and ensure the integrity of the purchasing process.²⁴

2.18 On 27 June 2014, the Clean Energy Regulator released for public consultation an exposure draft of the Carbon Abatement Contract to be used for the Emissions Reduction Fund and an accompanying discussion paper. Submissions are due by 18 July 2014.²⁵

Safeguarding emissions reductions

2.19 An Emissions Reduction Fund safeguard mechanism will be operational from 1 July 2015. Consultation on the design of the mechanism will continue to occur through 2014 and the first half of 2015. The mechanism will be put in place to ensure that 'emissions reductions paid for by the Emissions Reduction Fund are not displaced by a significant rise in emissions elsewhere in the economy'. It will be implemented through discrete legislation.²⁶

Other changes to the Carbon Farming Initiative

2.20 As outlined in the previous chapter, the Carbon Farming Initiative currently applies only to land-based emissions reduction projects and particular waste projects. The bill opens up the initiative to all sectors of the economy, whether on land, at sea or in Australia's external territories. The Explanatory Memorandum lists some of the new projects to reduce emissions which could be supported by the Emissions Reduction Fund, such as improving the energy efficiency of homes and industrial facilities, reducing electricity generator emissions, reducing waste coalmine gas, upgrading vehicles and improving transport logistics.²⁷

2.21 The bill alters the permanence arrangements for carbon sequestration projects. Under the existing legislation, sequestration projects must continue for 100 years. If a project does not fulfil this obligation, its carbon credits are relinquished. The bill permits new sequestration projects to nominate for a 25-year or 100-year permanence period. Projects that are currently subject to a 100-year permanence period can elect to convert to a 25-year period within two years of the commencement of the Emissions Reduction Fund. Information about a project's permanence period will be available through the Emissions Reduction Fund Register, which will assist both prospective buyers of land where sequestration projects are operating and buyers of credits from sequestration projects.²⁸

24 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 54.

25 Clean Energy Regulator, *News and Updates*, <http://www.cleanenergyregulator.gov.au/About-us/news-and-updates/Pages/default.aspx> (accessed 3 July 2014).

26 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 7.

27 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, pp 5–6; see also The Hon Greg Hunt, Minister for the Environment, *House of Representatives Hansard*, 18 June 2014, p. 12.

28 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, pp 66–67.

2.22 The bill proposes to change the timing of requirements relating to obtaining consent from 'eligible interest holders'. Currently, consent is required during the application stage for projects. The bill proposes that proponents of carbon sequestration projects may apply to receive conditional registration for their projects, prior to obtaining the consent of all parties with an eligible interest holding. This allows project proponents to simultaneously begin the process of registration a project and contacting the relevant eligible interest holders. Full registration of a project will not be granted until eligible interest holders have given their consent.²⁹

Transitional arrangements for existing Carbon Farming Initiative projects

2.23 Projects that are already registered under the Carbon Farming Initiative will be automatically registered under the Emissions Reduction Fund. Carbon Farming Initiative methodologies will also continue to apply unless varied or revoked.³⁰ Until 1 July 2015, proponents will be able to apply to register their projects using the eligibility rules and assessment methodologies that existed prior to the commencement of the bill.³¹

2.24 Projects transitioning from the current Carbon Farming Initiative arrangements to the Emission Reduction Fund will receive a second crediting period—that is, their current crediting period will end and a new crediting period will begin the day after the commencement of the Emissions Reduction Fund legislation. The second crediting period will be seven years for emissions reduction projects or 25 years for sequestration projects.³² The bill proposes that a transitioning project cannot have more than two crediting periods.³³

29 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 27.

30 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 61 and Schedule 1, items 388 and 392.

31 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 62 and Schedule 1, items 388 and 392.

32 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, pp 61–63; see also Schedule 1, item 152 (proposed section 70).

33 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 33 and Schedule 1, item 152 (proposed subsection 70(5)).

Chapter 3

Key issues

Introduction

3.1 This chapter discusses key issues raised in submissions and evidence, including:

- support for the bill;
- changes to the crediting period;
- the safeguard mechanism;
- additionality and co-funding;
- the development of methodologies;
- the auction process;
- enforceability and contract terms;
- carbon sequestration projects; and
- eligible interest holder consent.

Support for the bill

3.2 The Clean Energy Regulator provided evidence to the committee on its experience of administering the Carbon Farming Initiative and the feedback it had received from participants in the scheme's first two years of operation. The Regulator noted:

After two years of experience and regular feedback from our clients, we have a better understanding of administering the act and our clients also have been able to explain where there are some streamlining opportunities and reporting opportunities that will not change the integrity of the credits that are issued or the scheme but can provide for improved participation.¹

3.3 The Regulator agreed that the changes proposed in the bill would improve the current legislation and respond to issues raised in participant feedback.

3.4 CO2 Australia stated in its submission that the passage of the bill would be essential, should the carbon pricing mechanism be repealed. CO2 Australia stressed the need for consistency in carbon abatement policy. It commented that any gap between the repeal of the carbon pricing mechanism and the commencement of the provisions in the bill would result in uncertainty for those sectors of the economy that are seeking to address climate change.²

1 Ms Chloe Munro, Chair and Chief Executive Officer, Clean Energy Regulator, *Committee Hansard*, 1 July 2014, p. 20.

2 CO2 Australia, *Submission 10*, p. 1.

3.5 CO2 Australia welcomed the move to provide a single framework for multiple emissions reduction activities and to streamline administration of the Carbon Farming Initiative through the bill.³

3.6 The Carbon Market Institute, the peak body representing a broad range of participants in the market, described the Emissions Reduction Fund as having 'real benefit in terms of being able to channel funding into abatement that could deliver a kick-start to the decarbonisation'.⁴ It emphasised that the level of interest in participating in the Emissions Reduction Fund should not be underestimated:

A lot of project proponents have invested a lot of time and money to go through the methodology development processes and be in a position where they can bid into the Emissions Reduction Fund.⁵

3.7 Australian Soil Management fully supported the amendments contained in the bill and welcomed the recognition of 'the potential contribution of soil carbon in meeting the objectives of the Emissions Reduction Fund'.⁶

3.8 The Cement Industry Federation (CIF) and National Lime Association of Australia (NLAA) endorsed the broad intent of the bill:

The development of a consistent, national regulatory framework—supporting the use of alternative (non-fossil based) fuels such as those derived from waste—would potentially allow the domestic cement and lime industries to increase abatement opportunities.⁷

3.9 The CIF and NLAA further supported the risk-based approach to auditing emissions reductions and the streamlining of methodologies proposed by the bill.⁸

3.10 Hydro Tasmania supported the aim of the bill to ensure targeted and efficient funding processes but cautioned against the Clean Energy Regulator being too prescriptive and 'setting absolute guidelines that may prohibit important opportunities from progressing'.⁹

3.11 When asked what the effect would be on the land sector if the price on carbon were repealed and the Carbon Farming Initiative Amendment Bill were not passed, Carbon Farmers of Australia stated:

3 CO2 Australia, *Submission 10*, pp 1–2.

4 Mr Peter Castellás, Chief Executive Officer, Carbon Market Institute, *Committee Hansard*, 1 July 2014, p. 33.

5 Mr Peter Castellás, Chief Executive Officer, Carbon Market Institute, *Committee Hansard*, 1 July 2014, p. 34.

6 Australian Soil Management, *Submission 6*, p. 1.

7 The Cement Industry Federation and National Lime Association, *Submission 7*, p. 2.

8 The Cement Industry Federation and National Lime Association, *Submission 7*, p. 3.

9 Hydro Tasmania, *Submission 8*, p. 2.

...we would be forced into a sort of niche market type situation that would have more difficulties.¹⁰

Crediting period

3.12 There was some discussion in submissions and evidence about the changes the bill makes to crediting periods. CO2 Australia expressed concern that the bill removes the ability to re-credit projects after the initial crediting period expires. CO2 Australia noted that this has particular relevance for carbon sequestration or reforestation projects. It stated:

...the proposed legislation curtails the potential economic life of carbon assets that would continue to actively sequester carbon beyond the period for which the project is credited.¹¹

3.13 CO2 Australia recommended that a second 25-year crediting period be allowed for sequestration projects that have 100-year permanence.¹²

3.14 The Aboriginal Carbon Fund highlighted the effect that the single crediting period imposed by the bill would have on savanna burning projects:

They are not like energy efficiency projects where you make the change and there is a continuing benefit. Savanna projects require a continuing effort every year to manage the burning.¹³

3.15 The Kimberley Land Council called the change to a single crediting period 'significant'.¹⁴

3.16 The Carbon Market Institute acknowledged that the bill allows for some flexibility in the length of a crediting period and encouraged such an approach.¹⁵

3.17 The explanatory memorandum to the bill explains the single crediting period as follows:

This will ensure that the Emissions Reduction Fund continues to target new projects that build on previous gains.¹⁶

3.18 In response to consultation on the Carbon Farming Initiative Amendment Bill draft legislation, the Government has stated it will monitor the progress of savanna burning projects under the Emissions Reduction Fund and will review arrangements

10 Mrs Louisa Kiely, Director, Carbon Farmers of Australia, *Committee Hansard*, 1 July 2014, p. 36.

11 CO2 Australia, *Submission 10*, p. 2.

12 CO2 Australia, *Submission 10*, p. 2.

13 Aboriginal Carbon Fund, *Submission 5*, p. 2.

14 Kimberley Land Council, *Submission 12*, p. 3.

15 Carbon Market Institute, *Submission 11*, p. 8.

16 Carbon Farming Initiative Amendment Bill 2014, *Explanatory Memorandum*, p. 33.

for these projects as a priority as part of the operational review of the Emissions Reduction Fund at the end of 2015.¹⁷

Safeguard mechanism

3.19 As outlined in the previous chapter, the explanatory memorandum to the bill states that a safeguard mechanism for the Emissions Reduction Fund will begin on 1 July 2015, following consultation with stakeholders, and will be governed by discrete legislation.

3.20 CO2 Australia expressed the view that a legislative requirement to deliver the Emissions Reduction Fund safeguard mechanism by July 2015 should be included in the current bill.¹⁸

3.21 The Carbon Market Institute also observed that consideration of the safeguard mechanism would be beneficial at the commencement of the Emissions Reduction Fund. The Carbon Market Institute stated:

Although the draft legislation does not include the safeguard mechanism proposed in the ERF [Emissions Reduction Fund] White Paper, it is important to consider it at this stage to ensure that in implementation the ERF and the safeguard mechanism are linked. This will be crucial to ensure any new policy is enduring and can effectively limit Australia's emission growth to 2020 and beyond.¹⁹

3.22 It suggested that the safeguard mechanism include the allocation of baselines and that the costs of emissions reductions be transferred ultimately to the buyers of ACCUs:

If allocated baselines for entities covered under the safeguard mechanism are reduced over time, it transfers the 'heavy lifting' to meet emissions reduction targets to covered entities, rather than the tax payer funded ERF. The cost for emissions reduction is transferred to those who are required to buy the credits.²⁰

3.23 The Grattan Institute mentioned in its evidence the difficulty in setting baselines when no historical data exists—that is, for new businesses or businesses that engage in new practices.²¹

3.24 Regarding the development of the safeguard mechanism, the Department of the Environment confirmed that 'there is further work to be done' in 2014 but reported

17 Department of the Environment, *The Emissions Reduction Fund: the results of consultation on draft legislation*, <http://www.environment.gov.au/system/files/pages/7aef9f12-8ba1-4d9a-bf6a-1bc89a0bd6f5/files/erf-exposure-draft-legislation-consultation.pdf> (accessed 4 July 2014).

18 CO2 Australia, *Submission 10*, p. 2.

19 Carbon Market Institute, *Submission 11*, p. 4.

20 Carbon Market Institute, *Submission 11*, p. 5.

21 Mr Tony Wood, Program Director, Energy, Grattan Institute, *Committee Hansard*, 1 July 2014, p. 43.

that 'quite a bit of consultation with business' had occurred in the course of developing the Green Paper and the White Paper.²²

3.25 The department indicated that discussions so far had included the types of entities the mechanism covers and the historical basis on which baselines are set.²³ It stated that:

...the government's policy is actually to have safeguard baselines set at a level based on historical levels so that they prevent any increase in emissions beyond what business as usual might have been. It is not...to drive those baselines down to impose costs and therefore incentivise companies to undertake reductions to avoid those costs.²⁴

3.26 The department reiterated that the Government would continue to consult on appropriate baselines and compliance arrangements prior to the implementation of the safeguard mechanism. It confirmed that the Government would:

...continue to talk to business about what sorts of flexible compliance arrangements would be available in the event that baselines are breached by an entity.²⁵

Additionality and co-funding

3.27 Organisations involved in savanna burning in northern Australia emphasised the importance of the Carbon Farming Initiative to the continuation of their projects but raised a number of concerns about the provisions of the bill. The first was eligibility. The Carbon Farming Initiative Amendment Bill 2014 requires that emissions reduction projects be additional to business-as-usual activities, must not have started and must not be funded by other Government programs. The Aboriginal Carbon Fund expressed concern about these provisions:

...it could mean that we are ruled ineligible and that would mean wiping out a source of income that is worth hundreds of thousands of dollars and employs hundreds of traditional owners...²⁶

3.28 This view was supported by the Kimberley Land Council, which stated in its submission:

Land sector carbon abatement projects offer an opportunity to complement and strengthen existing Ranger activities with projects to reduce emissions

22 Mr Trevor Power, Acting First Assistant Secretary, Emissions Reduction Taskforce, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 56.

23 Mr Trevor Power, Acting First Assistant Secretary, Emissions Reduction Taskforce, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 56.

24 Mr Trevor Power, Acting First Assistant Secretary, Emissions Reduction Taskforce, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 51.

25 Mr Trevor Power, Acting First Assistant Secretary, Emissions Reduction Taskforce, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 56.

26 Mr Rowan Foley, General Manager, Aboriginal Carbon Fund, *Committee Hansard*, 1 July 2014, p. 23.

or store carbon on the land. Under the additionality requirements in the ERF Bill, these groups could be prevented from participation in carbon projects. This overlooks the fact that the funding they receive focuses on a much larger range of land management activities that do not include carbon abatement activities, and that, without funding from the ERF or CFI, they would not have the resources nor capacity to undertake carbon projects.²⁷

3.29 The Carbon Market Institute commented in its submission that the requirement that projects be new, additional and not co-funded needed clarification. It pointed out that savanna burning projects rely on co-funding from several Government programs and, without further explanation of these points, 'they may be considered non-additional and excluded from participating in the ERF'.²⁸

3.30 The Law Council of Australia supported the call for clarification and noted that the additionality and co-funding requirements have the potential to disadvantage Indigenous communities.²⁹ It suggested in evidence that the legislation could make specific provision for Indigenous land management practices:

We would even support the idea of a separate test of additionality applying to those sorts of projects.³⁰

3.31 The Department of the Environment acknowledged in its evidence to the committee that Indigenous land management could involve a range of Government programs. It pointed out that, while these programs support various aspects of land management, savanna burning activities receive support only through the Carbon Farming Initiative. Therefore, they should continue to be supported under the Emissions Reduction Fund. The department stated:

There is a sort of common-sense element to it. If another government program has funded something and the project is happening anyway, it would not be a good use of taxpayer funding to fund it again. But the government have made it quite clear that it is not their intention to prevent people from pooling together support from a range of different sources. Particularly in Indigenous areas, there will be a whole range of government programs that might touch on or intersect with something under the Emissions Reduction Fund.

The government know[s] that, on their own, none of those individual projects are sufficient to get savanna burning projects off the ground. The legislation talks about not funding projects that would already happen under another government program. In this case, savanna burning activity does not happen despite all the other government programs that you have in place. So it is clearly a case where funding is needed through the Emissions Reduction Fund to have those projects go ahead. The regulator will put out

27 Kimberley Land Council, *Submission 12*, p. 2.

28 Carbon Market Institute, *Submission 11*, p. 7.

29 Law Council of Australia, *Submission 17*, p. 3.

30 Mr Greg McIntyre SC, Law Council of Australia, *Committee Hansard*, 1 July 2014, p. 10.

further guidance to explain how it is that they will make that assessment on a case-by-case basis.³¹

3.32 Hydro Tasmania welcomed the bill's focus on ensuring that projects funded under the Emissions Reduction Fund be additional to normal business practices but advocated flexibility. It recommended that the assessment of projects for inclusion in the Emissions Reduction Fund take into consideration the influence of geographic location.³²

Development of methodologies

3.33 The Aboriginal Carbon Fund and the Kimberley Land Council commented in their submissions that the bill gives the minister an increased ability to propose and develop methodologies and expressed concern at this.³³ The Kimberley Land Council called it a 'top-down approach' and recommended:

...to facilitate continued innovation, the ERF Bill should allow the public to develop and propose methodologies, including variations and amendments to existing methodologies.³⁴

3.34 The Law Council of Australia observed that the current Carbon Farming Initiative framework provides opportunities for project proponents to suggest innovation in methodologies and that 'the ERF Bill will remove this ground-up approach and replace it with a 'top down' approach'—that is, one determined by the minister. It was of the view that, while the bill could streamline the assessment and endorsement of methodology proposals, it could make participation in the Emissions Reduction Fund difficult for some groups and could 'inadvertently stifle innovation and research and development'.³⁵

3.35 CO2 Australia expressed the view that the bill did not greatly expand the minister's responsibility for the development of methodologies and that it 'perhaps might simply be clearer'. It said in evidence:

This bill really does introduce the opportunity to have energy efficiency technologies, other forms of industrial abatement, subject to a rigorous methodology in the same way that the land sector is, and then those projects can essentially be part of the marketplace as a whole, so I think there is an advantage to that. It offers companies more opportunity to explore the space.³⁶

3.36 The Department of the Environment reported that it had consulted with a range of stakeholders on changes to methodology development and that ministerial

31 Ms Maya Stuart-Fox, Assistant Secretary, Legislation and Policy Frameworks Branch, Department of the Environment, *Committee Hansard*, 1 July 2014, pp 56–57.

32 Hydro Tasmania, *Submission 7*, p. 2.

33 Aboriginal Carbon Fund, *Submission 5*, p. 3; and Kimberley Land Council, *Submission 12*, p. 4.

34 Kimberley Land Council, *Submission 12*, p. 4.

35 Law Council of Australia, *Submission 17*, p. 5.

36 Dr Chris Mitchell, Managing Director, CO2 Australia, *Committee Hansard*, 1 July 2014, p. 6.

discretion had 'not been a significant concern'. It pointed out that, under the current legislation, the minister already decides whether or not to make a methodology determination. The department stated:

...there might be some misunderstandings about the extent of the changes in the legislation. In the current CFI act, a decision to make or not to make a methodology determination is a decision for the minister, so the minister has that discretion. The minister continues to have the role of deciding whether or not to make a methodology determination. As legislative instruments they are subject to parliamentary scrutiny, so there is that very important parliamentary scrutiny process.³⁷

3.37 The department reported that it had listened to stakeholder feedback about the development of methodologies. It said:

There was quite a lot of feedback from various stakeholders about the time required to develop and assess methodologies. We undertook a range of stakeholder consultation processes around methodology development. So a number of the changes that you see reflected in the legislation are a response to stakeholder feedback.³⁸

3.38 In addition, the department highlighted the ability for stakeholders to have input into the development of methodologies. It observed:

These methodologies under the Emissions Reduction Fund will be developed through technical working groups. There is information provided about the work of the technical working groups through, for example, an Emissions Reduction Fund newsletter. The membership of those technical working groups or access to information about what the technical working groups are doing is very open. They are collaborative processes. So there are lots of opportunities for people to make their views known and to have input into it.³⁹

3.39 The department stated that the amending legislation not only allows stakeholder input into methodology development, via technical working groups, but also allows the minister to propose methodologies that have been seen to be successful in other schemes. As under the current legislation, methodologies must meet the offsets integrity standards and the minister will continue to be advised by the Emissions Reduction Assurance Committee (formerly the Domestic Offsets Integrity Committee). The department stated:

So if, for example, the minister was interested in a methodology that had been developed from another scheme—the Clean Development Mechanism or another offset scheme overseas—the minister could ask...the emissions

37 Ms Maya Stuart-Fox, Assistant Secretary, Legislation and Policy Frameworks Branch, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 48.

38 Ms Maya Stuart-Fox, Assistant Secretary, Legislation and Policy Frameworks Branch, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 48.

39 Ms Maya Stuart-Fox, Assistant Secretary, Legislation and Policy Frameworks Branch, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 48.

assurance committee to assess that methodology and advise him on whether or not that method is suitable under the Emissions Reduction Fund...⁴⁰

3.40 The department also noted that the bill provides the ability 'to establish priorities for methodology development' and that this had come about in consultation with stakeholders through technical working groups. It said:

...there is an ongoing...work program for methodology priorities. That...would also be a collaborative process where, for example, industry or proponents could bring forward an idea that they would like to develop a methodology around a particular area. Then, effectively, the minister could consider that and consult with industry themselves about whether they would like to pursue that sort of methodology proposal and then, for example, publish a list of priorities where further methods could be developed.⁴¹

3.41 The department further stated:

So the process of prioritising it collaboratively in consultation with business means that there is a transparent process of thinking through what really are the priorities, what are the methods that we need to bring forward the biggest sources of low-cost emissions reductions.⁴²

Auction process

3.42 The Aboriginal Carbon Fund was of the view that the proposed auction process did not appear to be transparent.⁴³ The Kimberley Land Council, similarly, commented on the apparent lack of transparency in the auction process:

Without transparent and up-front information on the likely price for abatement, Indigenous communities will not be in a position to undertake the advanced planning—including feasibility assessments—required to participate in the ERF.⁴⁴

3.43 The Cement Industry Federation and National Lime Association of Australia expressed some concern at the possible administrative burden created by the auction process and suggested 'that a tender process be considered as the key instrument to select projects until the proposed review at the end of 2015'.⁴⁵

3.44 The Grattan Institute gave evidence that 'using reverse auctions is a perfectly viable way of reducing emissions, possibly at moderate cost', but that greater detail on

40 Ms Maya Stuart-Fox, Assistant Secretary, Legislation and Policy Frameworks Branch, Department of the Environment, *Committee Hansard*, 1 July 2014, pp 48–49.

41 Mr Trevor Power, Acting First Assistant Secretary, Emissions Reduction Taskforce, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 49.

42 Ms Maya Stuart-Fox, Assistant Secretary, Legislation and Policy Frameworks Branch, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 49.

43 Aboriginal Carbon Fund, *Submission 5*, p. 3.

44 Kimberley Land Council, *Submission 12*, p. 5.

45 The Cement Industry Federation and National Lime Association, *Submission 7*, p. 3.

the setting of baselines and the limit of funding needed to be provided. The Institute also noted that absence of detail about the safeguard mechanism could affect the auction process and the quality of bids.⁴⁶

3.45 The Clean Energy Regulator described the auction process as 'a very simple process to start with', where price would be 'the sole criterion'. The Regulator reported in its evidence to the committee that it would verify that each participant is proposing a credible amount of abatement.⁴⁷ It stated:

So the intention is to have a competitive auction process but also a process which encourages people to make their offers on realistic and conservative assumptions...⁴⁸

3.46 The Department of the Environment noted that it 'would ultimately be up to proponents to bid in what they see as a fair return or the cost of their project, and the auction process would determine whether they were successful'.⁴⁹

Enforceability and contract terms

3.47 The committee heard evidence from a number of witnesses on the options for enforcing compliance for projects registered under the Emissions Reduction Fund. CO2 Australia was of the view that compliance via contract provisions was preferable to legislation.⁵⁰

3.48 The Law Council of Australia echoed this view, commenting that statutory penalties were 'not a particularly helpful approach' and that 'the better approach would be for there to be a contractual relationship set up which would create a commercial obligation'.⁵¹

3.49 The Clean Energy Regulator informed the committee that it had released a draft Emissions Reduction Fund contract for consultation and that 'it is a commercial contract like any other', with 'the obligations on the supplier to deliver and the obligations on the purchaser to pay'.⁵² It stated that, while the bill allows more flexibility in reporting and auditing for project proponents, 'that does not relieve them

46 Mr Tony Wood, Program Director, Energy, Grattan Institute, *Committee Hansard*, 1 July 2014, pp 41 and 43–44.

47 Ms Chloe Munro, Chair and Chief Executive Officer, Clean Energy Regulator, *Committee Hansard*, 1 July 2014, p. 16.

48 Ms Chloe Munro, Chair and Chief Executive Officer, Clean Energy Regulator, *Committee Hansard*, 1 July 2014, p. 19.

49 Mr Trevor Power, Acting First Assistant Secretary, Emissions Reduction Taskforce, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 53.

50 Dr Chris Mitchell, Managing Director, CO2 Australia, *Committee Hansard*, 1 July 2014, pp 4–5.

51 Mr Greg McIntyre SC, Law Council of Australia, *Committee Hansard*, 1 July 2014, p. 11.

52 Ms Chloe Munro, Chair and Chief Executive Officer, Clean Energy Regulator, *Committee Hansard*, 1 July 2014, pp 16–17.

of the obligation to demonstrate that they have delivered the abatement, and it does not change our opportunities to examine that before issuing the credits'.⁵³

3.50 The Aboriginal Carbon Fund commented in its submission that the proposed five-year contract periods were too short, thus compounding 'the problem with the single crediting period'.⁵⁴

3.51 The Carbon Market Institute suggested aligning the five-year contract period and the seven-year crediting period. It proposed that this would offer 'more certainty and less risk' as projects might not otherwise find a buyer for their Australian carbon credit units in the remaining two years after the end of the contract. The Institute was also of the view that:

If the contract period is too short, clearly it will be more difficult to get finance...⁵⁵

3.52 In its evidence, the Department of the Environment explained that the Government was still consulting with the market on the contract length but that its preference was for five-year contracts. It explained that this approach was to provide 'certainty to proponents' that they would receive 'five years of credits at a fixed price', while giving them the ability to sell credits to other proponents in the market for the final two years.⁵⁶

Carbon sequestration

3.53 The committee received evidence related to the change the bill makes to permanence obligations for carbon sequestration projects. The Wentworth Group of Concerned Scientists stated that the proposed change from a 100-year permanence period to a 25-year period would 'weaken the permanence obligations'.⁵⁷ It also pointed to a lack of understanding about 100-year permanence, stating that it 'does not mean the land is locked up' and that 'if you want to change the land use you simply buy a carbon credit for the amount of carbon you would be replacing'.⁵⁸

3.54 Carbon Farmers of Australia supported the move from a 100-year to a 25-year permanence period. Carbon Farmers stated that it had 'spent many hours with the department' and that:

53 Ms Chloe Munro, Chair and Chief Executive Officer, Clean Energy Regulator, *Committee Hansard*, 1 July 2014, p. 16.

54 Aboriginal Carbon Fund, *Submission 5*, p. 3.

55 Mr Peter Castellás, Chief Executive Officer, Carbon Market Institute, *Committee Hansard*, 1 July 2014, p. 31.

56 Mr Trevor Power, Acting First Assistant Secretary, Emissions Reduction Taskforce, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 52.

57 Mr Peter Cosier, Director and Member, Wentworth Group of Concerned Scientists, *Supporting Statement*, 1 July 2014, p. 2.

58 Mr Peter Cosier, Director and Member, Wentworth Group of Concerned Scientists, *Committee Hansard*, 1 July 2014, p. 42.

The 25-year rule is one of the ones we have fought hard for.⁵⁹

3.55 Carbon Farmers of Australia reported that engaging in projects with a 100-year permanence period was seen by their members as 'pure risk' and that 'the fear was palpable'. It commented that, with the proposed introduction of the 25-year permanence period, 'people are starting to understand how the process can be less punitive'.⁶⁰

3.56 The ability to aggregate carbon sequestration projects under the changes to the legislation was also welcomed by Carbon Farmers of Australia. It was of the view that this 'takes away the fear that people will be left to stand on their own and face the consequences of disasters they could not control'.⁶¹

3.57 The Department of the Environment noted in its evidence that the White Paper emphasised the importance of project aggregation to pool 'small-scale sources of emissions'. It observed that the legislation removes 'potential barriers to sequestration' and makes the 'aggregation of land sector projects simpler'.⁶²

Eligible interest holder consent

3.58 A point raised by the Law Council of Australia in its evidence to the committee was that the bill allows a proponent to conditionally register a project, go to auction and be granted a contract before obtaining the consent of eligible interest holders. The Law Council commented that this could lead to a proponent spending time and money on a project that was ultimately unsuccessful due to a lack of consent from the eligible interest holders.⁶³

3.59 The Law Council also raised the need to seek consent from native title holders, highlighting that differences could exist between 'exclusive-possession native title and those who have a non-exclusive possession native title'.⁶⁴ Given the complexities of identifying native title holders, the Law Council advised obtaining their consent early in project planning.

3.60 The Department of the Environment clarified for the committee that the conditional registration provision was in response to requests from proponents to speed up the process by allowing the registration and auction process to take place while consent was being sought from eligible interest holders. It stated:

59 Mrs Louisa Kiely, Director, Carbon Farmers of Australia, *Committee Hansard*, 1 July 2014, p. 37.

60 Mr Michael Kiely, Director, Carbon Farmers of Australia, *Committee Hansard*, 1 July 2014, p. 38.

61 Mr Michael Kiely, Director, Carbon Farmers of Australia, *Committee Hansard*, 1 July 2014, p. 38.

62 Ms Maya Stuart-Fox, Assistant Secretary, Legislation and Policy Frameworks Branch, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 56.

63 Mr Greg McIntyre SC, Law Council of Australia, *Committee Hansard*, 1 July 2014, pp 8–9.

64 Mr Greg McIntyre SC, Law Council of Australia, *Committee Hansard*, 1 July 2014, p. 10.

The reason that change was made was because proponents were saying it takes a long time to go and get the consents and if we have to do that without having gone through the auction yet then we can waste a lot of time and money without knowing yet whether or not we are successful at auction. So they will go through auction and then finalise those consents.⁶⁵

3.61 The Clean Energy Regulator confirmed that the change to obtaining eligible interest holder consent is a matter that has 'been raised by stakeholders variously to ourselves and the department'. It commented that the change means that 'the proponent has a greater period of time in which to seek consent because often it can take some time'.⁶⁶

3.62 Notwithstanding this change, the Regulator stressed that the requirement to obtain eligible interest holder consent is 'absolutely clear' and it advises proponents to consider it at the planning stage of a project. The Regulator said that if a proponent chooses to proceed without that consent, 'they have accepted that risk'.⁶⁷

3.63 The Department of the Environment supported the Regulator's evidence that projects would not receive credits without the consent of eligible interest holders. It stated:

The way it works is that they cannot receive any credits until those consents are in place. The regulator has indicated that it would be a conditioned precedent under the contract: the contract would not come into effect until those consents were in place, and they cannot receive credits until those consents are in place.⁶⁸

Committee comment

3.64 The committee supports the Carbon Farming Initiative Amendment Bill 2014 as a key component of the Government's response to climate change.

3.65 The establishment of the Emissions Reduction Fund will expand and streamline the Carbon Farming Initiative. This will not only result in significant benefits to land-based carbon abatement projects but open up the scheme to innovative projects in all sectors. The committee considers that this is an important element in the Government's aim to reduce emissions at lowest cost. This will benefit business and the Australian community as a whole.

3.66 The committee further notes that the bill will deliver a smooth transition for proponents of carbon abatement projects registered under the current Carbon Farming

65 Ms Maya Stuart-Fox, Assistant Secretary, Legislation and Policy Frameworks Branch, Department of the Environment, *Committee Hansard*, 1 July 2014, pp 55–56.

66 Ms Mary-Anne Wilson, General Manager, Carbon Farming, Clean Energy Regulator, *Committee Hansard*, 1 July 2014, p. 14.

67 Ms Chloe Munro, Chair and Chief Executive, Clean Energy Regulator, *Committee Hansard*, 1 July 2014, p. 15.

68 Ms Maya Stuart-Fox, Assistant Secretary, Legislation and Policy Frameworks Branch, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 56.

Initiative and an essential ongoing market for credits in the event the carbon pricing mechanism is repealed.

3.67 The committee acknowledges that there has been widespread consultation in the development of the legislation and that this consultation is continuing with regard to methodology development, contract periods and the design of the safeguard mechanism, which will commence on 1 July 2015.

3.68 In addition, the committee considers that the Clean Energy Regulator has the expertise and resources to commence the administration of the Emissions Reduction Fund immediately.

Recommendation 1

3.69 The committee recommends that the Carbon Farming Initiative Amendment Bill 2014 be passed.

**Senator Anne Ruston
Chair**

Labor Senators' Dissenting Report

1.1 Labor Senators are deeply concerned that the Coalition Government is desperate for the Parliament to pass the Clean Energy Legislation (Carbon Tax Repeal) Bill 2013 and associated bills while the alternative Direct Action policy remains incomplete.

1.2 The Coalition announced its Direct Action policy in 2010. There has been limited information provided about the policy since this announcement, and very little support for the policy from within the science and economic communities.

1.3 The Direct Action policy includes a number of elements, all asserting to contribute to Australia's emissions reduction target of 5% on 2000 emissions levels by 2020. The elements of Direct Action include extending the Carbon Farming Initiative, planting 20 million trees, establishing the Green Army and the so-called centrepiece, the Emissions Reduction Fund.

1.4 The Coalition Government is seeking to amend the *Carbon Credits (Carbon Farming Initiative) Act 2011* to allow for the Emissions Reduction Fund to be administered. The Amendment allows for the Clean Energy Regulator to enter into contracts as part of the Emissions Reduction Fund administration and expands coverage of the carbon farming initiative to the entire economy.

1.5 The current Carbon Farming Initiative has been a bipartisan policy since it was introduced by the then Labor Government as part of the Clean Energy Package in 2011.

Emissions Reduction Fund

1.6 The Emissions Reduction Fund is based on a reverse-auction to purchase carbon pollution abatement. The 2014–15 Budget allocated \$1.14 billion across the forward estimates for the ERF. The Government insists up to \$2.55 billion is available for purchasing abatement, however has been unclear how this money is appropriated as it is not allocated in the Budget papers.

The ERF is based on three principles:

- Lowest cost emissions reduction: the reverse-auction will prioritise projects that propose emissions reductions per lowest cost, rather than per emissions reduction quantity or per industry.
- Genuine emissions reduction: the ERF will only support projects that would not have already been undertaken. However the definition means that projects that have been fully planned for will qualify. There has been no detail on the safeguard mechanism to ensure companies will not receive ERF money for projects they would have done regardless of the ERF.

- Streamlined administration: The ERF will be administered by the Clean Energy Regulator. The Government does not propose to increase staff resources at the Clean Energy Regulator for this task.

1.7 The development of the Emissions Reduction Fund has included multiple community and industry consultation sessions, as well as community consultation on the ERF Green Paper before the ERF White Paper was released in May and enabling legislation was brought to the House of Representatives. However, there are still very many aspects of the ERF that attract significant criticism within the community and it appears little effort has been made to address these concerns through the process.

1.8 A recent Senate Inquiry into Direct Action received 106 submissions and held five public hearings. The Committee did not hear from one representative that could categorically conclude the ERF will achieve its abatement targets within its existing budget.

1.9 Further, during both the May 2014 Budget Estimates hearings and the hearings into this Bill, the Department of the Environment admitted to being unsure as to the policy's success, citing the policy's current incomplete state as the reason for being unable to confirm its contribution towards the 5% emissions reduction target.

1.10 A number of eminent Australian economists and carbon market research agencies have released modelling to discredit the Government's claims of Direct Action's effectiveness, the predominant criticisms are summarised in this Dissenting Report.

1.11 For a full view of Federal Labor's views on this matter this dissenting report should be read in conjunction with the majority report from the March 2014 Senate Environment and Communications References Committee inquiry 'Direct Action: Paying polluters to halt global warming?'.

"Support for the Bill" but No Debate on the Bill

1.12 The Key Issues chapter of the Chair's Report into this Bill commences not by seeking to clarify technical issues raised in submissions but with a section seeking to highlight "Support for the Bill", particularly in the still hypothetical scenario of the abolition of the carbon price mechanism.

1.13 A large number of the Chair's questions during the public hearing focussed on ascertaining political "Support for the Bill".

1.14 Despite the prominence of this section in the Chair's Report and the reporting date of 7 July 2014, the Senate programme for the sitting week commencing 7 July 2014 does not list this Bill for debate.¹

1 Department of the Prime Minister and Cabinet: Legislative Drafting Program for the Senate, <http://www.dpmc.gov.au/parliamentary/senate/html/senate.html> (accessed Friday 4 July 2014).

1.15 However, the programme lists the Clean Energy Legislation (Carbon Tax Repeal) Bill 2013 and associated bills as the first order of business on 7 July 2014. The reporting date for these Bills is 14 July 2014.

Recommendation 1

1.16 If the Coalition Government truly considers the evidence provided by industry in answers to the Government's own rhetorical questions as of such a high concern, Labor Senators recommend that the Government delays the debate on the Clean Energy Legislation (Carbon Tax Repeal) Bill 2013 and associated bills until such time that it is prepared to also debate the Carbon Farming Initiative Amendment Bill 2014 in the Senate.

Key criticisms of the Emissions Reduction Fund and the Bill

There is insufficient funding to be able to secure enough abatement to meet Australia's emissions targets now and into the future

1.17 Recent research from Reputex shows that even if the full \$2.55 billion is used to buy abatement, the Government will fall 300 million tonnes short of its carbon emissions reduction targets.²

1.18 Former Treasury secretary Ken Henry and leading Australian economist Ross Garnaut have said that it's likely to cost up to \$5 billion to reach the target with the ERF.³

1.19 The underfunding issue was reinforced during the hearing by Mr Peter Castellanos Chief Executive Officer of the Carbon Market Institute who said that the ERF will not be the policy mechanism that is going to achieve the emissions reduction target⁴ and Mr Tony Wood Program Director Energy at the Grattan Institute who said that he has not seen any analysis that suggests that the ERF will be sufficient to meet the target⁵.

1.20 Despite the widespread concerns about the ability of the ERF's current budget to meet the target, Mr Trevor Power Acting First Assistant Secretary at the

2 Reputex, *High benchmark price to lift supply, but ERF short*, 11 June 2014, <http://www.reputex.com/media-centre/media-release-emissions-reduction-fund-to-be-undersupplied-reputex/> (accessed 4 July 2014).

3 ABC 7.30 Report, *Former Treasury head warns tax reform needed to pay for policy promises*, 12 March 2014, <http://www.abc.net.au/7.30/content/2014/s3962156.htm> (accessed 4 July 2014); Professor Ross Garnaut, *Submission 105*, Senate Environment and Communications References Committee *Inquiry into the Abbott Government's Direct Action Plan*, pp 1–8.

4 Mr Peter Castellanos, Carbon Market Institute, *Committee Hansard*, 1 July 2014, p. 32.

5 Mr Tony Wood, Grattan Institute, *Committee Hansard*, 1 July 2014, p. 42.

Department of the Environment confirmed that no estimates about emissions reductions under the ERF have been released.⁶

1.21 Further, in evidence at the hearing, the Chair and Chief Executive Officer of the Clean Energy Regulator, Ms Chloe Munro confirmed concerns that the \$2.55 billion budgeted for the ERF in the budget could be paid out for emissions reductions achieved post-2020.⁷

1.22 Mr Wood from the Grattan Institute and Mr Power from the Department of the Environment both confirmed that emissions reductions achieved post-2020 from ERF funding would not count towards the 2020 target.⁸

1.23 Mr Castellás proposed that to maximise pre-2020 reductions, the Clean Energy Regulator could construct the first auctions with a weighting on reductions in the pre-2020 period.⁹

1.24 Labor Senators are concerned that despite the clear concerns of a number of witnesses and highly reputable researchers and economists that the funding allocation for the Emissions Reduction Fund to 2020 is insufficient to meet the target, the Key issues section of the Chair's Report did not mention ERF funding once.

1.25 Labor Senators are concerned that no estimates about emissions reductions under the ERF have been released.

1.26 Labor Senators are concerned that the underfunded ERF does not include a policy that all emissions reductions financed from the fund must be achieved before 2020.

There is a lack of a robust safeguard mechanism with stringent baselines and penalties for exceeding baselines

1.27 The Government recently announced the safeguard element of the ERF will not start until 1 July 2015, despite the Government aiming to begin purchasing emissions under the ERF from 2014.

1.28 This is due to uncertainty about the design of the safeguard mechanism, with many industry representatives citing the difficulty to set benchmarks and enforce emissions reductions without legislation.

1.29 The Chair's Report noted that the Government is still consulting with business (despite the development of Green and White Papers) on the design of the safeguard mechanism.

6 Mr Trevor Power, Department of the Environment, *Committee Hansard*, p. 52.

7 Ms Chloe Munro, Clean Energy Regulator, *Committee Hansard*, 1 July 2014, p. 20.

8 Mr Tony Wood, Grattan Institute, *Committee Hansard*, 1 July 2014, p. 43; Mr Trevor Power, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 57.

9 Mr Peter Castellás, Carbon Market Institute, *Committee Hansard*, 1 July 2014, p. 32.

1.30 Labor Senators note from the White Paper that the safeguarding mechanism will cover facilities with direct emissions of 100,000 t CO₂-e or more per annum but there appears to be confusion as to how many businesses this equates to.

1.31 Mr Power from the Department of the Environment said in evidence to the hearing that the government estimates about 190 companies might be engaged by the safeguard mechanism.¹⁰

1.32 While the April 2014 White Paper stated that around 130 businesses will be covered by the safeguard mechanism.¹¹

1.33 The Chair's Report includes the Grattan Institute's evidence on the difficulty in setting baselines when historical data does not exist, but does not elaborate on the potential risks to covered entities from growth in uncovered emissions as highlighted in the Australian Industry Greenhouse Network's submission.

AIGN draws attention to the Government's intent for the mechanism to ensure emissions reductions paid for through the ERF are not displaced by significant rises elsewhere in the economy. The safeguarding mechanism will leave about 48 per cent of Australia's emissions uncovered, creating the possibility for economy-wide emissions to rise outside the scope of the mechanism. Entities covered under the safeguarding mechanism must not bear the burden of rises in uncovered emissions in any way.¹²

1.34 Mr Peter Castellanos, Chief Executive Officer, Carbon Market Institute summarised the potential effectiveness of a safeguard mechanism with penalties in evidence to the hearing:

Using the safeguard mechanism will be necessary to defray the ongoing indefinite public cost of funding emissions reduction and become the primary means to manage emissions growth across the economy.

Importantly, there needs to be a legislated make-good provision or penalty for companies liable under the mechanism that exceed their allocated baseline. This could be in the form of purchasing eligible units, either Australian carbon credit units or international units or a combination of both.

As the Emissions Reduction Fund funding reduces over time and the allocated safeguard mechanism baselines become more stringent, the policy framework could transfer to a more efficient market based scheme where the cost to the economy to meet our targets will progressively move from the public to the private sector.

Setting declining baselines will also increase the incentive for companies to limit emissions growth and to invest in low carbon technologies or

10 Mr Trevor Power, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 56.

11 Department of the Environment: Emissions Reduction Fund White Paper, http://www.environment.gov.au/system/files/resources/1f98a924-5946-404c-9510-d440304280f1/files/emissions-reduction-fund-white-paper_0.pdf p. 52, (accessed 4 July 2014).

12 Australian Industry Greenhouse Network, *Submission 14*, p. 3.

processes, which is consistent with driving sustained decarbonisation of major emitting sectors.

Businesses need policy certainty regarding future compliance obligations to ensure that they are not competitively disadvantaged in the period 2020 to 2030 as the emission reduction task intensifies.¹³

1.35 The submission from Dr Tim Moore a Director at NetPositive highlighted the inadequacy of information in the Green and White Papers on the safeguard mechanism, the need for a market for emission reduction units to enable Australia to meet its abatement obligations over the coming decades and the potential opportunities for carbon farming.¹⁴

1.36 Labor Senators urge the Government to complete development of the safeguard mechanism prior to the first auction, including stringent baselines and penalties for exceeding baselines.

There is no legislated limit or 'cap' on Australia's emissions in line with emissions reductions targets

1.37 The most effective way to ensure Australia meets its emissions reduction targets is to place a legal cap on pollution.

1.38 The ERF, as it stands, is a voluntary program which businesses can choose to participate in.

1.39 There is no disincentive for businesses to continue their usual practices which could lead to increased carbon pollution.

1.40 As outlined in the previous section, the Government expects between 100 – 200 companies to be subject to the safeguard mechanism, which will cover only approximately 52 percent of Australia's emissions.

1.41 The NetPositive submission notes that a cap and trade system would be the most preferred model but even a baseline and credit approach would be preferable to the current proposed arrangements and went on to say:

The ERF and CFI legislation need a clear example of how a national cap will be imposed to create an emissions limit, enabling the development of a market based approach to lowest cost projects driving the emissions reductions.¹⁵

1.42 The Chair's Report provided no commentary on the need or otherwise for a legislated limit or 'cap' on Australia's emissions.

13 Mr Peter Castellanos, Carbon Market Institute, *Committee Hansard*, 1 July 2014, pp 29–30.

14 NetPositive, *Submission 4*, p. 5.

15 NetPositive, *Submission 4*, p. 5.

1.43 Labor Senators urge the Government to include a legislated limit for 2020 and 2050 in its legislative package to reduce emissions to ensure a long term outlook is maintained for reducing Australia's carbon emissions.

There is no access to international emissions credits

1.44 The ERF is not connected to international emissions reduction schemes, limiting businesses' opportunities to participate in other schemes, which could potentially lead to cheaper emissions abatement opportunities for business.

1.45 The submission from the Australian Industry Greenhouse Network supported access to international units:

This will promote genuine emissions reductions, assist with maintaining Australia's competitiveness, and address the potential for leakage.¹⁶

1.46 The AIGN submission went on to state that in respect to the make-good provision:

One option is to enable entities needing to make good a shortfall to access the international market; this would alleviate industry concerns that participation in the ERF could inadvertently be a cost-negative exercise.¹⁷

1.47 In its submission to this inquiry, the Carbon Market Institute also highlighted the benefits of including eligible international units in the make-good provision:

The international market is established, deep and liquid and would allow proponents to be able to effectively manage delivery risk should the ACCU secondary market not develop. In this scenario, the proponent would only be paid the contract price for the ACCUs delivered. They would not be paid for any of the make-good international units delivered so there would not be any arbitrage opportunity.¹⁸

1.48 Many submissions to the References Committee inquiry queried whether this was the best approach including; the Grattan Institute, Sustainable Energy Association, Australian Industry Group, Professor David Karoly, Professor Frank Jotzo, Investor Group on Climate Change, Mr John Hawkins, Carbon Market Institute, Mr James Wight and Corporate Carbon Advisory.¹⁹

1.49 Labor Senators consider that it is appropriate for Australia to utilise international emissions credits as a proportion of its emissions reduction policy mix.

16 Australian Industry Greenhouse Network, *Submission 14*, p. 2.

17 Australian Industry Greenhouse Network, *Submission 14*, p. 5.

18 Carbon Market Institute, *Submission 11*, p. 12.

19 Senate Environment and Communications References Committee, *Inquiry into the Abbott Government's Direct Action Plan*, p 117.

The maximum terms of contracts for purchasing emissions reductions under the Emissions Reduction Fund need to be increased

1.50 The ERF contracts are capped at five years.

1.51 Businesses have said this is not enough time to implement large-scale projects that will lead to large-scale emissions reductions.

1.52 The current five-year contract does not present an attractive investment opportunity for businesses that will be required to provide their own funds for projects such as infrastructure upgrades or a transition to renewable energy sources.

1.53 The Chair's Report notes concerns from two submissions, the Aboriginal Carbon Fund and the Carbon Market Institute around the proposed contract length.

1.54 Labor Senators note that a number of other submissions were also concerned by the proposed short contract length.²⁰

1.55 Labor Senators are concerned that the evidence provided by the Department around the Government's expectations on a participant's return on capital are at odds with a number of submissions.²¹

1.56 Labor Senators urge the Government to reconsider the short contract length and work with potential contractors in the lead up to the first auction to address these concerns.

Ongoing emissions reductions projects must have a renewal option for crediting period

1.57 The existing Carbon Farming Initiative allows for an application to renew crediting periods after the first crediting period has expired.

1.58 However, this Bill proposes to limit crediting periods to one single period (with the exception of limited transitional projects).

1.59 The Government has decided to only grant projects one crediting period on the basis that it wants the Emissions Reduction Fund to target new projects that build on previous gains.

1.60 The Chair's Report does not outline why the Government has taken this position.

1.61 The Chair's Report very briefly mentions the concerns of three submissions, the Aboriginal Carbon Fund, the Kimberley Land Council and C02 Australia, misrepresents the concerns of the Carbon Market Institute (in seeking to find a

20 Australian Sustainable Built Environment Council, *Submission 3*, p. 2; Australian Industry Greenhouse Network, *Submission 14*, p. 3; CSIRO, *Submission 16*, p. 3; NetPostive, *Submission 4*, p. 2.

21 Mr Trevor Power, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 52.

supportive submission) and disregards the concerns of NetPositive and the Law Council of Australia.²²

1.62 The Carbon Market Institute's submission included the following criticism of limiting projects to one crediting period:

Limiting projects to one crediting period may impact the formation of a liquid secondary market in ACCUs and in particular limiting the term of this market. For example, a project with a single seven-year crediting period and a five-year ERF contract would only be able to generate a further two years' worth of ACCUs to supply into the secondary market. The potential for limited liquidity in ACCU secondary market would make it more difficult to manage the risk of makegood provisions required for ERF contract under delivery. This may result in project proponents under-bidding volume and a higher average cost per tonne for the ERF. The development of the voluntary market may also be inhibited by lack of liquidity as the inability to generate ACCUs beyond the single seven- or 15-year crediting period would limit supply into this market.²³

1.63 The submission from NetPositive was equally as damning in its assessment of the one crediting period policy:

There is no sound reason nor any logical policy setting for the Government to limit successful proponents to only one contracting period. This policy actually undermines the potential for the ERF to drive new investment in dealing with Australia's abatement challenge. If a project has a crediting lifetime greater than the contract lifetime, then the project or credit owners should be able to bid into subsequent rounds.²⁴

1.64 The submission from the Kimberly Land Council is much more comprehensive than calling the change to the single crediting period "significant" as quoted in the Chair's Report:

This change undermines business certainty and removes the opportunity for Indigenous communities to develop long-term sustainable businesses based upon carbon projects. The change puts at a significant disadvantage existing CFI projects that have made business decisions based on the assumption that future crediting periods would be available.²⁵

1.65 Labor Senators note the Government has not presented a credible reason to change current policy in this area and urge the Government to keep the current renewal terms.

22 Carbon Market Institute, *Submission 11*, p. 8; NetPositive, *Submission 4*, p. 2; Law Council of Australia, *Submission 17*, p. 7.

23 Carbon Market Institute, *Submission 11*, p. 8.

24 NetPositive, *Submission 4*, p. 2.

25 Kimberley Land Council, *Submission 12*, p. 3.

There is significant confusion and concern around the new additionality requirements

1.66 The existing Carbon Farming Initiative provides for additionality in a number of ways.

1.67 However, this Bill proposes to remove the common practice test, and introduce a requirement that projects must be new and unlikely to occur as a result of another government programme.

1.68 The Chair's Report highlights that a number of submissions were concerned about the change in additionality requirements and seeks to allay these concerns through an explanation from the Department.

1.69 The Chair's Report particularly focusses on the legitimate concerns of the Aboriginal Carbon Fund, Kimberley Land Council, Carbon Market Institute and Law Council of Australia that indigenous savannah burning, which relies on other government funding may not meet the new additionality test. This view was also raised in the submission from the Indigenous Land Council.²⁶

1.70 Mr Greg McIntyre, Chair, Australian Environment and Planning Law Group at the Law Council of Australia clarified the Council's concern:

Our real concern is that it is not entirely clear whether they might often fail the test. So we suggest that some careful attention be given to it so that it is made clear that they are unlikely to fail the test.²⁷

1.71 The Chair's Report includes evidence from the Department of the Environment that these issues will be dealt with on an ad-hoc basis through the regulator.

1.72 The Chair's Report fails to include the concerns of the Australian Sustainable Built Environment Council that under the proposed changes, retrofitting existing plant and equipment and utilising other government incentives where private funding is still required are not additional.²⁸

1.73 Mr Cosier from the Wentworth Group of Concerned Scientists responded to a question from Senator Milne regarding low-till or no-till agriculture meeting the new additionality definition that in this case Government will not actually paying for carbon abatement, but providing a subsidy to agriculture.²⁹

1.74 Ms Stuart-Fox from the Department of the Environment confirmed that the Department look at an activity on a fairly broad brush basis rather than necessarily looking at the particulars of whether a particular given activity could build soil carbon:

26 Indigenous Land Council, *Submission 13*, pp 3–4.

27 Mr Greg McIntyre, Law Council of Australia, *Committee Hansard*, 1 July 2014, p. 10.

28 Australian Sustainable Built Environment Council, *Submission 3, Attachment 1*, pp 8–9.

29 Mr Peter Cosier, Wentworth Group of Concerned Scientists, *Committee Hansard*, 1 July 2014, p. 46.

The recognition was that, while in some cases individual management actions will build soil carbon levels on a given property, they may not necessarily do so across the board. So the decision was made that, in order to incentivise positive action to build soil carbon, it was sensible to take this broader activity basis approach to the common-practice test.³⁰

1.75 Labor Senators are concerned that the Government is not looking to clarify its flawed amendments but deal with the confusion on an ad-hoc basis through the regulator. Ad-hoc determinations may not address these concerns, potentially stranding large savannah burning projects in particular.

1.76 Labor Senators urge the Government to clarify the new additionality requirements through amendments to this Bill.

The change from bottom up to top down methodology development

1.77 The existing Carbon Farming Initiative provides for methodology development by stakeholders through an advisory committee to the Minister.

1.78 However, this Bill proposes to remove this bottom up process and give the Minister sole responsibility for methodology development.

1.79 The Chair's Report highlights the Aboriginal Carbon Fund, the Kimberley Land Council and Law Council of Australia's evidence against this proposal and uses evidence from C02 Australia that does not seem to relate to methodology development together with evidence from the department in support of the change.

1.80 While the evidence from the department attempts to justify the change, it does not take into consideration the potential for small stakeholders to be overlooked in the process.

1.81 The submission from the Aboriginal Carbon Fund expands on this issue:

While private developers can still make suggestions, the Government will call the shots and decide which methodologies are developed and endorsed. This will stifle entrepreneurship from the land sector. For example, we have invested in developing a methodology for savanna enrichment – growing bush foods and carbon at the same time – but will it ever be put to the Minister under the new system?³¹

1.82 In evidence to the hearing, Mr Foley expanded on the work of ACF to develop the savanna enrichment methodology:

It has taken three years of research and development. We work quite closely with Dr Mark Dangerfield, who is an expert in this field and a former member of the Domestic Offsets Integrity Committee, the DOIC.

There is a trial plot up in Broome that the Kimberley Training Institute have had for the last several years. We put in a draft for consultation through the

30 Ms Maya Stuart-Fox, Department of the Environment, *Committee Hansard*, 1 July 2014, p. 54.

31 Aboriginal Carbon Fund, *Submission 5*, p. 3.

department. They were pretty happy with it. We had to do one or two things to it, tidy it up a little bit, and we have formally submitted it to the DOIC now.

I must admit I am at a loss to know what the process is from here. They sent me back an email saying, 'Thank you very much.' I do not know when it is going to be approved or where it is up to. I know there is a 40-day consultation period. But with these tools that we use in the tool kit, there needs to be a clear process that says within six months they must be either approved or rejected. At the moment, there seems to be a bit of a black hole there.

I do not understand why it is up to the minister to put forward methodologies, and from the department. We live in a social democracy and we have excellent scientific researchers. We have CSIRO and AIMS and a whole range of scientific people who can develop these methodologies—and we are one of them. We have done it and we can see that there is a technique that can be used to bring the country to back to producing food and carbon credits. I am not sure that the minister and the department are going to be the font of all wisdom when it comes to scientific endeavour.³²

1.83 Labor Senators are concerned that the Government is seeking to centralise control for the development of methodologies with the Minister, which submissions quite rightly raise may stifle innovation and preclude small stakeholders.

1.84 Labor Senators urge the Government to urgently revisit the process for methodology development.

An increase of staffing may be required within the Clean Energy Regulator in order to administer the scheme properly

1.85 The Government proposes the entire scheme will be administered by the Clean Energy Regulator, including running the reverse auction and implementing the safeguard mechanism, if and when that comes on line, in addition to its existing regulatory functions.

1.86 The Government does not propose to increase the staff resources of the Regulator.

1.87 The Chair's Report does not mention staffing of the Clean Energy Regulator until the final comment, which states that "the committee considers that the Clean Energy Regulator has the expertise and resources to commence the administration of the Emissions Reduction Fund immediately".

1.88 Labor Senators note that the Chair's Report only includes phrase "to commence the administration..." and does not express confidence that the Clean Energy Regulator has the resources to administer the scheme in the long term.

32 Mr Rowan Foley, Aboriginal Carbon Fund, *Committee Hansard*, 1 July 2014, p. 26.

1.89 Labor Senators note that at 30 June 2013 the Clean Energy Regulator had a total staff of 371, while in evidence to the hearing, Ms Munro confirmed that the latest numbers were 317 full-time equivalent staff, with funding for 339 full-time equivalent staff.³³

1.90 Labor Senators are concerned that this Bill and the resulting Emissions Reduction Fund will create considerable extra work for the Clean Energy Regulator, which may lead to delays in administration and potential oversights.

Labor's position on the Carbon Farming Initiative Amendment Bill 2014

1.91 This Bill amends the Carbon Farming Initiative Act to allow for the administration of the Abbott Government's Emissions Reduction Fund.

1.92 The Carbon Farming Initiative has previously enjoyed bipartisan support.

1.93 Since the first announcement of the Emissions Reduction Fund in 2010, there has not been any public support for the program. From the limited information available, it is clear this program is little more than a grants program. Eminent Australian economists have predicted the fund will not achieve its goals within its existing budget and carbon market research experts have supported these predictions with modelling showing the Government will fall well short of its emissions reductions targets.

1.94 There is no available modelling or research to support Government claims of the ERF's projected successful outcomes.

1.95 The Committee view section of the Chair's Report does not make a comment on the potential effectiveness or otherwise of the ERF as the so-called centrepiece of the Government's policy to reduce emissions by five percent on 2000 levels by 2020.

1.96 The policy's design has not been completed, and as a result the Government's own department is unsure of specific elements.

1.97 Industry representatives have repeatedly raised concerns at Senate inquiry hearings, community forums and in the media, while there's no evidence the Government has addressed these concerns.

1.98 Mr Wood from the Grattan Institute said in evidence at the hearing that in running auctions under the ERF before the issues are finalised there is a risk that the "best buyers" won't turn up.

You may very well get buyers turning up, but I suspect what you will not get is the lowest cost abatement, because of, firstly, the design flaws associated with baselines; secondly, to some extent, additionality; and,

33 Clean Energy Regulator, *Annual Report 2012–13*, p. 70; Ms Chloe Munro, Clean Energy Regulator, *Committee Hansard*, 1 July 2014, p. 16.

thirdly, the limited term of the contracts which the government is prepared to enter under the ERF.³⁴

1.99 There is reported discontent within Government backbenches about the cost of the policy, given its known shortfalls.

1.100 Based on the available information, Labor Party Senators do not expect the Emissions Reduction Fund will achieve Australia's international obligations to reduce its emissions by 5% on 2000 levels by 2020.

Recommendation 2

Labor Senators recommend that the Carbon Farming Initiative Amendment Bill 2014 not be passed.

**Senator Anne Urquhart
Senator for Tasmania**

**Senator the Hon Lisa Singh
Senator for Tasmania**

34 Mr Tony Wood, Grattan Institute, *Committee Hansard*, 1 July 2014, p. 44.

Additional Comments by the Australian Greens

1.1 The Australian Greens oppose in the strongest possible terms, the replacement of the Clean Energy Act 2011 with the Carbon Farming Initiative Amendment Bill 2014 (the Bill).

1.2 The greatest failure of the proposed legislation is that it is a short-term fix and incapable of being scaled up to meet our emissions reduction challenge without a massive burden on public expenditure. It would cost taxpayers billions of dollars to meet even mildly higher aspirations under an international agreement that will be negotiated up to the Paris Conference of the Parties next year.

1.3 The world expects Australia to do its fair share in limiting global warming to two degrees. The policy that is embodied in this legislation cannot come anywhere near this requirement.

1.4 Huge commercial opportunities currently exist for countries that are transitioning from a high pollution intensity economy into an efficient, low-carbon and prosperous one. The Carbon Farming Initiative Amendment Bill 2014 takes away any competitive advantages that Australia is currently developing and instead encourages businesses to be wasteful with its resources or to rely on government subsidies for its profitability.

1.5 Instead of the marketplace driving the innovations and productivity gains across multiple sectors of the economy, this bill will make government decision-makers responsible for choosing those advances in very limited sections of the economy.

1.6 It will not drive the transformational change necessary for Australia to prosper in a carbon constrained world faced with a climate change emergency for the following main reasons:

- (a) It is narrow. To achieve the lowest cost emission reductions, the bulk of the grant scheme will be focussed on energy efficiency. Despite the Minister's assurances, energy generation, mining and transport will be cast aside from Direct Action. Carbon farming will only be competitive if the integrity of the scheme is completely abandoned by giving absolute discretion to the Minister to vary the relevant methodologies.
- (b) It is unfinanceable because the grants are so small, contracts are limited to five years, payment is available only on completion and the prices on offer are so low that it falls far short of being investment grade. Finance institutions and banks will not waste their time to finance a project under the emissions reduction fund.
- (c) It is optional so there is no incentive for polluters to participate. The scheme will be underutilised by all except those best placed to receive easy subsidies. Low participation increases the cost of reducing emissions because of less competitive pressure. Furthermore any

reductions in emissions in one area of the economy will be lost by gains in another unregulated area.

- (d) It is costly because it requires a huge bureaucracy to administer the grant scheme. There will be very little emissions reductions for the amount of public money required to administer these expensive tasks.
- (e) It is economically illiterate because to achieve enough abatement to achieve the government's paltry 5% reduction target would require a carbon price of between \$20-40 but under the existing budget, the scheme could only pay \$3.60 per tonne.
- (f) It is pointless because those projects that are most likely to succeed under a reverse auction will be low-cost and have a short payback period, meaning they were the most likely to happen anyway, without the government's corporate welfare on offer.

1.7 In addition to these fundamental design flaws are the significant weakening of the methodologies that calculate how much carbon has been sequestered in the land.

1.8 Like the entire Direct Action policy, the mechanical framework has been painfully contorted in order to achieve superficial political objectives. In this case, the government's political objective is to make funds for carbon farming competitive against energy efficiency or capital upgrade projects. To achieve this, carbon farming rules have to be massively weakened in order to get public money out the door and into forestry projects similar to those driven by managed investment schemes under the Howard government.

1.9 The wide discretion provided to the minister under the Bill to allow projects to generate credits removes any guarantee that a tonne of carbon paid for does not end up in the atmosphere. This would result in the worst of both worlds, public money spent on abatement projects that have no identifiable environmental benefit.

1.10 To meet the UNFCCC Kyoto rules, Australia's policy framework must be rigorous. By giving the Minister huge discretion to undermine methodologies makes our compliance highly questionable and may make carbon credits ineligible in international markets.

1.11 Another area of serious concern is the removal of the prohibition on a project earning credits from the clearing of native forests or using material obtained from clearing a forest under s. 27(4)(j) of the Carbon Farming Initiative Act 2011 to be replaced with the requirement for the minister simply 'consider any adverse environmental impacts' would breach the Kyoto rules. Again the intention of the bill is to offer desperately needed revenue streams to the failing native forest logging industry.

1.12 Finally the Greens are concerned by the weakening of the additionality rules, the changes to the permanency requirements in order to allow 25 years of sequestration instead of 100 (25% of the time, but still 80% of the value) and the delinking of projects from Natural Resource Management plans.

Senator Christine Milne
Leader of the Australian Greens

Additional Comments by Senator Nick Xenophon

1.1 Australia cannot underestimate the challenges our environment, our economy and our way of life will face if we do not take proactive steps to manage climate change. We need to reshape our economy to move towards less carbon-intensive ways of operating across all sectors. It is a fine balance between using a carrot and a stick—something to support and encourage businesses and households, but also something to enforce measures where encouragement doesn't work. This needs to be carried out in the most cost effective way possible.

1.2 While I acknowledge the Government's proposed amendments to the Carbon Farming Initiative will go some of the way to reducing greenhouse gases there is currently too much uncertainty as to how effective this scheme will be.

1.3 For example, the Carbon Farming Initiative Amendment Bill 2014 ('the bill') proposes to limit the standard crediting period for emissions reduction projects to seven years. Unlike the current framework which allows for project proponents to reapply for accreditation after seven years, the bill removes this possibility. While there is provision for projects to receive accreditation for more than seven years through the design of methodologies, I believe this will do little to encourage investment in long term projects, particularly where initial capital costs are high. As the Carbon Market Institute told the committee:

There is a potential mismatch between the effective abatement generating periods of many carbon abatement assets and the single crediting periods as proposed in the Bill. For many projects, particularly land-based projects, a single seven- or 15-year crediting period is inadequate. Preventing abatement projects from generating ACCUs beyond these periods may have a number of implications on both the level of participation in the ERF and the general level of private sector investment in abatement projects.¹

1.4 I agree with the Carbon Market Institute proposal that crediting periods "should better align with the life of carbon abatement assets".² Whether the intended flexibility of the methodologies will achieve this is yet to be seen.

1.5 The absence of clear information as to how the proposed safeguard mechanism will look and operate is cause for serious concern. The Government must ensure that gains from carbon abatement and sequestration projects are not cancelled out by increases in emissions elsewhere. In order to achieve this, the safeguard mechanism must involve an immediate penalty and it must be directly linked to the Carbon Farming Initiative legislation. Without such a link there is a real danger the safeguard mechanism will not achieve its desired objective.

1 The Carbon Market Institute, *Submission 11*, pp 8–9.

2 The Carbon Market Institute, *Submission 11*, p. 6.

1.6 The concerns of the Grattan Institute in relation to the safeguard mechanism should also be heeded. During the public hearing Mr Anthony Wood from the Grattan Institute outlined some of these concerns:

Senator XENOPHON: Mr Wood, is it fair to say that without safeguard mechanisms in place now that will skew the scheme and cause a cost blow-out, both in terms of the cost of the budget and in that it will affect the achievability of the target?

Mr Wood: I think the simple answer to your question is yes. It is a serious problem relating not only to existing businesses that change their business activities but also to new businesses, the most obvious example being LNG businesses in Queensland—businesses for whom there are no obvious ways of even setting baselines. I have not seen anything tabled as yet that would solve that problem. So it is one of those absolutely fundamental design parameters around the ERF itself that suggest that achieving the target at lowest cost is still a significant challenge.³

1.7 While this bill is a step in the right direction in terms of Australia's climate change policy, it does require refinement.

Recommendation 1

1.8 The legislation should be amended to allow for longer contracting and crediting periods as well as an immediate and effective safeguard mechanism.

Senator Nick Xenophon
Senator for South Australia

3 Mr Anthony Wood, Program Director, Energy, Grattan Institute, *Committee Hansard*, 1 July 2014, p. 43.

Appendix 1

Submissions, additional information, and answers to questions taken on notice

Submissions

- 1** Country Carbon
- 2** Mr Stuart Box
- 3** Australian Sustainable Built Environment Council
- 4** Net Positive
- 5** Aboriginal Carbon Fund
- 6** Australian Soil Management
- 7** Cement Industry Federation
- 8** Hydro Tasmania
- 9** Climate Change Authority
- 10** CO2 Australia
- 11** Carbon Market Institute
- 12** Kimberley Land Council
- 13** Indigenous Land Corporation
- 14** Australian Industry Greenhouse Network
- 15** Carbon Farmers of Australia
- 16** CSIRO
- 17** Law Council of Australia

Additional information

Wentworth Group of Concerned Scientists (from public hearing, 1 July 2014, Canberra)

Answers to questions taken on notice

Department of the Environment (from public hearing, 1 July 2014, Canberra)

Law Council of Australia (from public hearing, 1 July 2014, Canberra)

Appendix 2

Public hearing

Tuesday, 1 July 2014 – Canberra

CO2 Australia

Dr Chris Mitchell, Managing Director

Law Council of Australia

Mr Greg McIntyre SC, Chair, Australian Environment and Planning Law Group

Clean Energy Regulator

Ms Chloe Munro, Chief Executive Officer

Ms Mary-Anne Wilson, General Manager, Carbon Farming

Dr Lesley Dowling, General Manager, Regulatory Assurance and Integrity

Aboriginal Carbon Fund

Mr Rowan Foley, General Manager

Mr Jeremy Dore, Project Development and Legal

Carbon Market Institute

Mr Peter Castellias, Chief Executive Officer

Carbon Farmers of Australia

Mrs Louisa Kiely, Director

Mr Michael Kiely, Director

Grattan Institute

Mr Tony Wood, Program Director, Energy

Wentworth Group of Concerned Scientists

Mr Peter Cosier, Director

Department of the Environment

Mr Trevor Power, Acting First Assistant Secretary, Emissions Reduction Fund Taskforce

Ms Shayleen Thompson, First Assistant Secretary, International and Land Division

Ms Maya Stuart-Fox, Assistant Secretary, Legislation and Policy Frameworks Branch

Ms Kristin Tilley, Assistant Secretary, Emissions Reduction Fund Taskforce

Mr James White, Assistant Secretary, Industrial Abatement Branch

Department of Agriculture

Mr Mark Tucker, Deputy Secretary

Mr Nico Padovan, First Assistant Secretary, Agricultural Adaptation and Forestry

Ms Julie Gaglia, Acting Assistant Secretary, Drought Policy and Reform

