2009

EXPOSURE DRAFT

CARBON POLLUTION REDUCTION SCHEME BILL 2009

COMMENTARY

(Circulated by the authority of the Minister for Climate Change and Water, Senator the Hon Penny Wong)

Note

The Commentary has been prepared for the purpose of assisting readers to understand the exposure draft of the Carbon Pollution Reduction Scheme Bill 2009. When the bills are introduced into Parliament, an explanatory memorandum will be tabled which may differ from this Commentary.

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Glossary

The following abbreviations and acronyms are used in this commentary.

Abbreviation	*Definition*
Authority	The Australian Climate Change Regulatory Authority
CO_2-e	Carbon dioxide equivalence
The draft bill	The draft Carbon Pollution Reduction Scheme Bill 2009
The draft consequential amendments bill	The draft Carbon Pollution Reduction Scheme (Consequential Amendments) Bill 2009
Eligible emissions unit	An Australian emissions unit or an eligible international emissions unit.
Eligible international emissions unit	A certified emission reduction (other than a temporary certified emission reduction or a long-term certified emission reduction), an emission reduction unit, a removal unit, a prescribed unit issued in accordance with the Kyoto rules.
Garnaut Climate Change Review Final Report; Garnaut Final Report	R. Garnaut, *The Garnaut Climate Change Review: Final Report*, Cambridge University Press, 2008
Green Paper	*Carbon Pollution Reduction Scheme Green Paper*, July 2008
IPCC	Intergovernmental Panel on Climate Change
Kyoto unit	An assigned amount unit, a certified emission reduction, an emission reduction unit, a removal unit or a prescribed unit issued in accordance with the Kyoto rules.
Kyoto rules	This term is defined in section 5. In brief, it includes the Kyoto Protocol, decisions of the Meeting of the Kyoto

Abbreviation	***Definition***
	Parties, certain standards adopted by such a Meeting and prescribed instruments.
NEMMCO	The National Electricity Market Management Company
Non-Kyoto international units	A prescribed unit issued in accordance with an international agreement (other than the Kyoto Protocol) or a prescribed unit issued outside Australia under a law of a foreign country.
OTN	Obligation transfer number
Registry	National Registry of Emissions Units
The Scheme	The Carbon Pollution Reduction Scheme
White Paper	*Carbon Pollution Reduction Scheme: Australia's Low Pollution Future*, White Paper, December 2008

General outline

Rationale for the Carbon Pollution Reduction Scheme

Climate change is the greatest social, economic and environmental challenge of our time. Scientific evidence confirms that human activities, such as burning fossil fuels (coal, oil and natural gas), agriculture and land clearing, have increased the concentration of greenhouse gases in the atmosphere. As a consequence, the earth's average temperature is rising and weather patterns are changing. This is affecting rainfall patterns, water availability, sea levels, storm activity, droughts and bushfire frequency, putting at risk Australian coastal communities, health outcomes, agriculture, tourism, heritage and biodiversity for current and future generations.(1)

The climate is already changing, with more frequent and severe droughts, rising sea levels and more extreme weather events. Thirteen of the 14 warmest years since records began occurred between 1995 and 2008 (2), and Australia has experienced warmer than average mean annual temperatures for 17 of the past 19 years.(3) The latest report from the Intergovernmental Panel on Climate Change (IPCC), the 2007 Fourth Assessment Report, concludes that Australia has significant vulnerability to the changes in temperature and rainfall projected over the coming decades.(4)

The Garnaut Climate Change Review Final Report paints a bleak picture of Australia at the end of this century should greenhouse gas emissions continue unchecked. There would be major declines in agricultural production across much of the country. The Great Barrier Reef and other reef systems, such as Ningaloo, would be effectively destroyed, with serious ramifications for tourism industries and biodiversity. Coastal infrastructure would be at risk of damage from storm surges and flooding. Key Australian export markets would have significantly lower economic activity, feeding back into lower prices for Australian exports and poorer terms of trade.

The Garnaut Final Report suggests that emissions are tracking at the upper bounds of the scenarios modelled by the IPCC in the Fourth Assessment Report. New data and scientific understanding, unavailable for the Fourth Assessment Report, suggest that the rate and magnitude of climate change over the next century may be at the high end of the range estimated by the IPCC. Trends in global mean temperature and sea-level rise are also at the upper end of the range of projections.(5) There is increasing concern

about the stability of the Greenland and west Antarctic ice sheets, with major implications for sea-level rise.(6)

The costs of inaction on climate change

The IPCC's Fourth Assessment Report suggests that, in a 'business as usual' world where world-wide economic growth continues, based on fossil fuels, the best estimate of temperature rise by the end of the century would be 4 degrees Celsius.(7) The report says that climate change caused by this temperature rise is very likely to have widespread and severe consequences, including significant species extinctions around the globe, increased danger of wildfire, real threats to food production, and severe health impacts, with dramatic increases in morbidity and mortality from heatwaves, floods and droughts.(8)

The environmental impacts of climate change have flow-on effects for other aspects of human society, such as the economy, security and human health.

Referring to Australia's region, the Lowy Institute for International Policy has noted:

> … even if not catastrophic in themselves, the cumulative impact of rising temperatures, sea levels and more mega droughts on agriculture, fresh water and energy could threaten the security of states in Australia's neighbourhood by reducing their carrying capacity below a minimum threshold, thereby undermining the legitimacy and response capabilities of their governments and jeopardising the security of their citizens. Where climate change coincides with other transnational challenges to security, such as terrorism or pandemic diseases, or adds to pre-existing ethnic and social tensions, then the impact will be magnified.(9)

While some climate change is unavoidable, the negative effects of warming can be substantially diminished by prompt and concerted action. The sooner we stabilise and then reduce atmospheric concentrations of greenhouse gases, the sooner we can reduce our impact on the climate and minimise the risk of dangerous change.

Small variations in climate are expected to be more damaging to Australia than to other developed countries. Climate change will also affect Australia's neighbours.

Australia's economic growth in recent years has boosted domestic living standards and consumption. This growth has been supported by rapidly expanding developing economies, particularly in the Asia-Pacific region.

Continued growth in developing economies could be threatened by the impacts of climate change as expenditure is diverted to cope with severe weather events, food crop failures, droughts and population displacement.

The findings of the Garnaut Final Report suggest that, in the long term, the costs of inaction will be greater than the costs of mitigation. The aggregate costs of action are modest, and the benefits of action (and the cost of inaction) increase over time, becoming more pronounced in the second half of this century and beyond.

Analysis presented in the Garnaut Final Report builds a strong case for responding to climate change with mitigation action. The Garnaut Final Report observes that 'the overall cost to the Australian economy is manageable and in the order of one tenth of 1% of annual economic growth'(10) and concludes that 'the costs of well-designed mitigation, substantial as they are, would not end economic growth in Australia, its developing country neighbours or the global economy; unmitigated climate change probably would'.(11)

The Garnaut Final Report also predicts that, in a world of unmitigated climate change, real wages will be 12% lower by 2100 than in a world without climate change. This is due to the reduced demand for labour in the second half of the century as a result of climate change.

The Government accepts the key findings of the Garnaut Climate Change Review Final Report that:

- a fair and effective global agreement delivering deep cuts in emissions consistent with stabilising concentrations of greenhouse gases at around 450 parts per million or lower would be in Australia's interests

- achieving global commitment to emissions reductions of this order appears unlikely in the next commitment period

- the most prospective pathway to this goal is to embark on global action that reduces the risks of dangerous climate change and builds confidence that deep cuts in emissions are compatible with continuing economic growth and improved living standards.

Economies can respond more efficiently to new circumstances when businesses and individuals have certainty about long-term direction. Starting as soon as possible on a gradual adjustment to a low-carbon economy will give them the opportunity to plan their adjustment pathways and manage changes in technology, equipment and skills requirements,

and will minimise the risk of stranding existing long-lived assets (12). This will help to reduce the costs of mitigation.

The Australian community stands to gain from a comprehensive response to climate change. Modelling conducted by the CSIRO suggests that taking action to reduce Australia's greenhouse gas emissions could catalyse strong jobs growth over the next 10 years – in the transport, construction, agriculture, manufacturing and mining sectors.(13) A comparison can be drawn with the process of Australian tariff reform.

In addition, Australia has experience in developing and implementing trading schemes (such as the Greenhouse Gas Abatement Scheme) and is well placed to provide the necessary financial services to support developing carbon markets in the Asia-Pacific region.

The Government's climate change strategy

The Government's climate change policy is built on three pillars—reducing Australia's carbon pollution, adapting to the impacts of climate change that we cannot avoid, and helping to shape a global solution.

Reducing Australia's carbon pollution

The Government has committed to a medium-term national target range of reducing emissions by between 5% and 15% of 2000 levels by 2020, and a long-term emissions reduction target of 60% below 2000 levels by 2050.

Meeting the emissions reductions targets will be challenging. Australia's emissions have been growing rapidly since 1995. Monitoring and reporting of Australia's emissions by the Department of Climate Change (14) suggest that, while Australia is likely to meet its Kyoto Protocol target of limiting emissions in the 2008–2012 period to an average of 108% of 1990 levels, emissions will increase to 120% of 1990 levels by 2020 (after the expanded Renewable Energy Target is taken into account) without additional policy measures. (15) This indicates considerable momentum in national emissions.

The Government will manage the transformation to a low-carbon economy through:

- the implementation of the Carbon Pollution Reduction Scheme (the primary tool for driving reductions in greenhouse gas emissions)
- an expanded national Renewable Energy Target

- investment in renewable energy technologies and in the demonstration of carbon capture and storage
- action on energy efficiency.

To avoid adverse income or distributional effects arising from the Scheme and ensure the most vulnerable households in society are protected, the Government is introducing changes to the tax and transfer systems and the introduction of new energy efficiency measures to help alleviate increases to the cost of living arising from the Scheme.

The Government has established the $2.15 billion Climate Change Action Fund to provide targeted assistance to business, community sector organisations, workers, regions and communities to smooth the transition to a low pollution economy. The Fund will assist in breaking down market barriers that may raise the cost of responding to a carbon price, and to encourage investment in low-emissions technology. It will also provide targeted assistance for sectors, businesses, regions, communities and workers that may be disproportionately affected by the introduction of the Scheme because of their economic reliance on industries that are more exposed to a carbon price.

The Fund will operate between 2009-2010 and 2012-13 (with an additional $300 million committed over the period 2013-14 to 2014-15).

Adapting to unavoidable climate change

Even if global mitigation efforts are successful, scientific evidence indicates that some climate change is unavoidable. The National Climate Change Adaptation Framework has been developed by the Australian Government and all State and Territory governments to build Australia's capacity to respond effectively to climate change, and outlines action to reduce regional and sectoral vulnerability.

Helping to shape a global solution

While Australia is responsible for only a relatively small proportion of global emissions, Australia's climate and economy are likely to be strongly affected by climate change. Australia therefore has a strong and direct national interest in pursuing a global solution. Being one of the group of countries leading the global response means that Australia is in a position to positively shape an international agreement to address climate change beyond the first compliance period of the Kyoto Protocol, which ends in 2012. Australia's domestic action will also be a critical influence on our international credibility and capacity to help shape an effective global response.

Major steps to date

United Nations Framework Convention on Climate Change

The United Nations Framework Convention on Climate Change was ratified by Australia on 30 December 1992. The Convention is aimed at stabilising greenhouse gas concentrations in the atmosphere at a level that would prevent dangerous anthropogenic interference with the climate system. It provides an overall framework for intergovernmental efforts, rather than setting binding emission reduction targets.

Ratification of the Kyoto Protocol

The Prime Minister handed over Australia's instrument of ratification of the Kyoto Protocol on 3 December 2007. The ratification entered into force on 11 March 2008. Under the Kyoto Protocol, Australia is committed to restraining its national emissions to an average of 108% of 1990 levels over the first commitment period (2008 to 2012).

Green Paper

On 16 July 2008, the Government released its Carbon Pollution Reduction Scheme Green Paper. This Paper reflected the Government's preferred positions on issues relating to the Carbon Pollution Reduction Scheme.

After the publication of this paper, the Government received more than 1000 submissions relating to all aspects of climate change policy. More than 2400 people attended 18 public consultation sessions and workshops held in capital cities and regional areas. More than 260 companies attended technical workshops and meetings. Six industries and non-government roundtables were held with representatives from 45 organisations.

White Paper

On 15 December 2008, the Government released its White Paper entitled *Carbon Pollution Reduction Scheme: Australia's Low Pollution Future*.

This reflected the Government's decisions on the scheme. It addressed, among other things, the national emissions trajectory and target, coverage, reporting and compliance, the nature of Australian emissions units, acceptable international units, auctioning, scheme caps, assistance, tax and accounting issues, household assistance and complementary measures, and the Climate Change Action Fund.

Public information sessions on the White Paper were held in capital cities in December 2008. On 26 February 2009, public information sessions were delivered through a Sky Channel broadcast to 37 regional centres.

The detailed policy positions in the White Paper are reflected in the package of draft bills that are being released for public comment.

The legislative package

The Government is releasing the following draft bills for public comment:

- Carbon Pollution Reduction Scheme Bill 2009
- Carbon Pollution Reduction Scheme (Consequential Amendments) Bill 2009
- Australian Climate Change Regulatory Authority Bill 2009
- Carbon Pollution Reduction Scheme (Charges – General) Bill 2009
- Carbon Pollution Reduction Scheme (Charges – Customs) Bill 2009
- Carbon Pollution Reduction Scheme (Charges – Excise) Bill 2009

The Carbon Pollution Reduction Scheme Bill 2009 is the main bill. It contains the detailed provisions relating to the emissions trading scheme. These include:

- entities and emissions that are covered by the scheme
- liable entities' obligation to surrender emissions units corresponding to their emissions
- limits on the number of emissions units that will be issued
- the nature of Australian emissions units
- allocation of Australian emissions units
- assistance in relation to emissions-intensive trade-exposed activities and coal-fired electricity generators

- voluntary inclusion of reforestation activities under the Scheme
- the National Registry of Emissions Units
- monitoring and enforcement.

The Carbon Pollution Reduction Scheme (Consequential Amendments) Bill 2009 includes some (but not all) of the consequential amendments which will be necessary, in particular amendments to the taxation legislation and to the *National Greenhouse and Energy Reporting Act 2007*, which will provide the basis for emissions reporting required under the Scheme. The remaining consequential amendments will be developed in the interval between release of the exposure draft and finalisation of the bill for introduction.

The Australian Climate Change Regulatory Authority Bill 2009 will establish the Australian Climate Change Regulatory Authority which will administer the trading scheme, the reporting regime (the *National Greenhouse and Energy Reporting Act 2007*) and the renewable energy regime (*Renewable Energy (Electricity) Act 2000*).

Three of the draft bills are technical bills, in case the charge for Australian emissions units issued as the result of an auction or for a fixed charge is, at some time in the future, considered to be taxation:

- Carbon Pollution Reduction Scheme (Charges – General) Bill 2009 will impose charges for the issue of Australian emissions units as the result of an auction or for a fixed charge *if* the charges are taxation within the meaning of section 55 of the Constitution but are neither duties of customs nor duties of excise.
- Carbon Pollution Reduction Scheme (Charges – Customs) Bill 2009 will impose charges for the issue of Australian emissions units as the result of an auction or for a fixed charge *if* the charges are taxation and are duties of customs within the meaning of section 55 of the Constitution.
- Carbon Pollution Reduction Scheme (Charges – Excise) Bill 2009 will impose charges for the issue of Australian emissions units as the result of an auction or for a fixed charge *if* the charges are taxation and are duties of excise within the meaning of section 55 of the Constitution

Some matters which need to be addressed in the legislation referred to above will be addressed in the interval between release of the exposure

draft and finalisation of the bills for introduction. There are, for example, several matters relating to reforestation which are in this category.

Other elements of the White Paper package which need to be implemented through legislation are expected to be introduced with the bills referred to above, although they are not being publicly exposed at the same time. This includes legislation to implement the household assistance package and a maritime levy on emissions from shipping services provided by vessels engaged in international voyages carrying domestic cargo and domestic passengers.

Outline of the scheme

The Carbon Pollution Reduction Scheme Bill 2008 (the bill) will establish a national emissions trading scheme, the Carbon Pollution Reduction Scheme (the Scheme).

The quantity of greenhouse gas emissions for which liable entities are responsible will be monitored, reported and audited.

At the end of each year, each liable entity will need to surrender an eligible emissions unit for every tonne of greenhouse gas emissions that they are responsible for in that year.

Eligible emissions units include Australian emissions units issued by the Australian Climate Change Regulatory Authority (the Authority) and eligible international emissions units. The number of Australian emissions units issued by the Authority in each year will be limited by a scheme cap.

Liable entities will compete to purchase the number of units that they require, either at auctions arranged by the Authority or on the secondary trading market. Those that value the units most highly will be prepared to pay most for them. For many liable entities, it will be cheaper to reduce emissions than to buy units.

Certain categories of entities will receive an administrative allocation of Australian emissions units, as a transitional assistance measure. Those entities will be able to use the units to comply with obligations under the Scheme or sell them.

The objects

The objects of the Scheme are specified in clause 3 of the draft bill. The first object is to give effect to Australia's obligations under the United

Nations Framework Convention on Climate Change and the Kyoto Protocol. The Carbon Pollution Reduction Scheme is designed as the key policy tool to meet Australia's international obligations regarding greenhouse gas emissions reductions.

The second is to support the development of an effective global response to climate change. The Scheme will contribute to the development of a global carbon market and put Australia in a position to influence the shape of the post-2012 international legal framework for climate change.

The Government accepts the key findings of the Garnaut Final Report that:

- A fair and effective global agreement delivering deep cuts in emissions consistent with stabilising concentrations of greenhouse gases at around 450 parts per million or lower would be in Australia's interests

- Achieving global commitment to emissions reductions of this order appears unlikely in the next commitment period

- The most prospective pathway to this goal is to embark on global action that reduces the risks of dangerous climate change and builds confidence that deep cuts in emissions are compatible with continuing economic growth and improved living standards.

The third object is to take action directed towards meeting Australia's targets of reducing greenhouse gas emissions to 60% below 2000 levels by 2050 and reducing greenhouse gas emissions to between 5% and 15% below 2000 levels by 2020, and to do this in a flexible and cost-effective way.

The range represents:

- A minimum (unconditional) commitment to reduce emissions to 5% below 2000 levels by 2020

- A commitment to reduce emissions by up to 15% below 2000 levels by 2020 in the context of global agreement under which all major economies commit to substantially restrain emissions and advanced economies take on reductions comparable to Australia.

The scheme in brief

National targets and Scheme caps

The Government has announced national targets which are reflected in the objects of the Scheme quoted above.

The Scheme is a 'cap and trade' scheme. It involves setting a national scheme cap for a particular year and issuing units within that cap. The scheme cap for a particular year is a quantity of greenhouse gases that have a carbon dioxide equivalence of a specified number of tonnes.

Scheme caps will be lower than the emissions path required to meet the national targets because some emissions sources are not covered by the Scheme (primarily, agricultural and deforestation emissions) and direct emissions from facilities are only covered if they exceed specified thresholds (usually 25,000 tonnes of carbon dioxide equivalence per year).

Detailed scheme cap numbers for each relevant financial year will be specified in regulations**.** The Government intends that these be consistent with the 2020 and 2050 targets. The Minister will be required to take all reasonable steps to ensure that regulations to specify the scheme cap numbers for the first five years of the Scheme are made before 1 July 2010. The purpose of this requirement is to provide market certainty. In a similar vein, for all subsequent financial years, the Minister is required to take all reasonable steps to ensure that regulations declaring the scheme cap number are in place at least five years before the end of the relevant year. There is provision for a default scheme cap number in the event that there is no scheme cap number for a year beginning on or after 1 July 2015.

To provide further guidance to liable entities and participants in the carbon market more generally, national scheme gateways may be prescribed for years beginning on or after 1 July 2015. A gateway is a range, comprising an upper bound and a lower bound of emissions, expressed in terms of tonnes of carbon dioxide equivalent, for a particular year. The Minister is required to take all reasonable steps to ensure that the scheme caps are within the range specified for the relevant year. The matters relevant to setting the gateways will be the same as in relation to setting national scheme caps.

The same considerations that are relevant in making decisions about national targets and the national emissions trajectory are relevant for setting caps and gateways. In making a recommendation to the Governor-General about scheme cap and scheme gateway regulations, the Minister must have regard to Australia's international obligations under the United Nations Framework Convention on Climate Change and the Kyoto

Protocol, and the most recent report of the independent review commissioned under this draft bill. Other matters relevant to setting the national scheme caps and gateways are specified in the draft bill and discussed in Chapter 2 of this commentary.

The draft bill is designed to provide the maximum feasible level of certainty over future scheme caps consistent with retaining legitimate flexibility to adapt to changing international conditions.

Liable entities and covered emissions

The Scheme applies liability in two main ways. First, liability generally arises where the greenhouse gases emitted from the operation of a facility has a carbon dioxide equivalence of 25,000 tonnes or more per year. (One exception is in respect of landfill facilities, where the threshold is 10,000 tonnes for facilities within a prescribed distance of another landfill facility accepting the same classification of waste). Where the entity that has operational control of the facility is a member of a controlling corporation's group, liability attaches to the controlling corporation. The controlling corporation's group consists of a controlling corporation and its subsidiaries, if any. To avoid doubt a group may consist of the controlling corporation alone. Where the legal person with operational control of the facility is not a member of a controlling corporation's group (a non-group entity), liability attaches to that person.

Secondly, where there are large numbers of small emitters, it is more practical to cover emissions by applying liability at another point along the supply chain. For example, to avoid imposing a compliance burden on many individual suppliers or users of fossil fuels and synthetic greenhouse gases, while sending the same price signal, the Scheme applies liability at the earliest point of the fuel supply chain within Australia, for example the importer or manufacturer of the fuel or synthetic greenhouse gas.

In some situations, entities that purchase fuel from that 'upstream' entity will be required to quote an 'obligation transfer number' and to take responsibility for emissions that would result from the combustion of the purchased fuel (referred to as 'potential emissions'). Large users of fossil fuels (other than petroleum liquid fuels) will be required to do this.

In certain other situations the purchaser will be allowed, on a voluntary basis, to obtain and quote an 'obligation transfer number', acquire the fuel, gas or other substance and take responsibility for surrendering the units to meet the Scheme obligation. This mechanism allows entities to take on liability voluntarily or to avoid liability for emissions associated with exported substances, such as export of black coal and synthetic greenhouse gases, because the emissions will occur outside Australia. This is discussed in detail in Chapter 1.

Making upstream entities liable, while providing the 'obligation transfer number' mechanism, will assist in achieving a reduction of greenhouse gas emissions in a flexible and cost-effective way.

Issue of Australian emissions units

The Australian Climate Change Regulatory Authority will issue Australian emissions units up to the national scheme cap each year. These units will be issued:

- following purchase through an auction (see Chapter 3)
- in relation to emissions-intensive trade-exposed activities (see Chapter 4)
- in relation to coal-fired electricity generators (see Chapter 5).

In addition, units will be issued:

- on application, for the first 5 years of the scheme, at a fixed charge (see Chapter 3)
- for reforestation (see Chapter 6)
- for the destruction of synthetic greenhouse gas (see Chapter 7).

Chapter 2 addresses Australian emissions units and eligible international emissions units.

Assessment and surrender

Liable entities under the Scheme will report the emissions for which they are liable through the *National Greenhouse and Energy Reporting Act 2007*. This Act will be amended to require those liable entities which are not currently reporting under that Act to do so.

Liability may arise from several sources for which the one entity is liable. For example, controlling corporation A may be responsible for the emissions from one or more facilities and as a large user of fossil fuels. The emissions from each of these sources are 'provisional emissions numbers'.

The sum of the provisional emissions numbers is reduced by any excess surrender number (ie excess units surrendered in the previous year) and increased by the 'make good' number (if the entity failed to meet its

obligations in a previous year). The result of this calculation is the entity's emissions number.

Eligible emissions units representing this number must be surrendered by 15 December following the relevant financial year. If sufficient units are not surrendered, a penalty becomes due on 31 January and a late payment penalty will begin to accrue. The penalty is a pecuniary penalty and a 'make good' obligation. (A 'make good' obligation means that if a liable entity surrenders too few units in one year, the obligation to surrender the shortfall carries over into the following year.)

This is explained in Chapter 8.

Compliance and enforcement

The powers relating to information gathering and monitoring are described in Chapter 9. The enforcement regime is also described in that Chapter.

The National Registry

A National Registry, described in Chapter 10, will be established to track the ownership of eligible emissions units and to manage their surrender and cancellation. This includes opening of accounts, and correction and rectification.

Public information

Price-relevant information will be published regularly to enable Scheme participants to make informed decisions about the price of emissions units. In addition, information about liable entities, holders of Registry accounts and forestry projects will be available. This is described in Chapter 11.

Independent reviews

An independent expert advisory committee will be constituted periodically to conduct public reviews of the Scheme. The committee and its operations are described in Chapter 12.

Review of decisions and miscellaneous

Chapter 13 addresses merits review of decisions by the Australian Climate Change Regulatory Authority and various miscellaneous matters.

Simplified outline

The draft bill includes a simplified outline of the Scheme (at clause 4) and each Part of the bill includes a simplified outline of that Part's contents.

Date of effect and application

While the proposed Act will commence 28 days after Royal Assent**,** the first year in relation to which entities will be liable under the Scheme will commence on 1 July 2010. This is achieved by use of the phrase 'eligible financial year' which is defined to mean the financial year beginning on 1 July 2010 or a later financial year.

Early commencement of the proposed Act will allow liable entities and the Authority to prepare for the Scheme and for the Authority to operate the National Registry in relation to Kyoto units. Preparation will include:

- Education and assistance for entities which are likely to be liable and their representatives
- Receipt and assessment of applications for, for example, certificates of eligibility for coal-fired generation assistance, registry accounts, obligation transfer numbers, emissions-intensive trade-exposed assistance and in relation to reforestation
- The holding of at least one auction.

Transitional provisions and consequential amendments

The transitional provisions and consequential amendments are included in the draft Carbon Pollution Reduction Scheme (Consequential Amendments) Bill. There is a separate commentary for this draft bill.

Financial impact; compliance cost impact; regulation impact statement

Statement as to financial impact and compliance cost impact will be available at the time of introduction. A Regulation Impact Statement will also be available at the time of introduction.

Proposal announced

The measures are based on the positions included in the White Paper entitled *Carbon Pollution Reduction Scheme: Australia's Low Pollution Future*, released by the Government on 15 December 2008.

Endnotes

(1) Intergovernmental Panel on Climate Change, *Fourth assessment report, Synthesis report*, 2007.

(2) Based on UK Climatic Research Unit Hadley Centre data.

(3) Based on Bureau of Meteorology data.

(4) Intergovernmental Panel on Climate Change, *Fourth assessment report, Synthesis report*.

(5) S Rahmstorf, A Cazenave, JA Church, JE Hansen, R Keeling, DE Parker & RCJ Somerville, 'Recent climate change observations compared to projections', *Science*, vol. 316, 2007, p. 709, doi: 10.1126/science.1136843.

(6) EJ Rohling, K Grant, CH Hemleben, M Siddall, BAA Hoogakker, M Bolshaw & M Kucera, 'High rates of sea level rise during the last interglacial period', *Nature Geoscience*, 2008, vol. 1, pp. 38–42.

(7) Intergovernmental Panel on Climate Change, *Fourth assessment report, Synthesis report*.

(8) Intergovernmental Panel on Climate Change, *Fourth assessment report, Synthesis report*.

(9) A Dupont & G Pearman, *Heating up the planet: Climate change and security*, Lowy Paper 12, Lowy Institute for International Policy, 2006.

(10) R Garnaut, *The Garnaut Climate Change Review: Final report*, Chapter 12.

(11) R Garnaut, *The Garnaut Climate Change Review: Final report*, Chapter 11.

(12) Stranded assets are those that are no longer economically viable due to a change in circumstance, even though they are viable from an engineering point of view.

(13) S Hatfield Dodds, G Turner, H Schandl & T Doss, *Growing the green collar economy: Skills and labour challenges in reducing our greenhouse emissions and national environmental footprint*, report to the Dusseldorp Skills Forum, CSIRO Sustainable Ecosystems, Canberra, 2008.

(14) Department of Climate Change, *Tracking to the Kyoto target: Australia's greenhouse emissions trends 1990 to 2008 2012 and 2020*, Commonwealth of Australia, 2008.

(15) Modelling conducted by the Australian Treasury (published in *Australia's low pollution future* (2008)) used scenarios to explore the potential economic effects of climate mitigation policy on Australia. Each scenario represents, in a stylised way, a different possible future, including levels of greenhouse emissions, which may differ from those projected in *Tracking to the Kyoto target*. The scenarios developed and presented by the Treasury in *Australia's low pollution future* are illustrative and do not represent the official policy or negotiating position of the Australian Government, are not an official Government or Treasury forecast, and are not an official projection of Australia's future greenhouse gas emissions.

Chapter 1
Liable entities and covered emissions

Outline of chapter

1.1 This Chapter deals with Part 3 of the draft bill.

1.2 Divisions 2, 3 and 4 of Part 3 of the draft bill set out the categories of liable entities that have obligations under the Scheme, and the sources of emissions for which these liable entities will have Scheme obligations.

1.3 Divisions 5 and 6 of Part 3 of the draft bill provide for mechanisms that enable entities to assume and transfer emissions obligations, and set out the circumstances in which these mechanisms can be used.

Context

1.4 The Scheme covers a broad range of emissions sources. This reduces the overall cost to the Australian economy of achieving emissions reductions, by increasing opportunities for low-cost abatement.

1.5 The Scheme will cover the stationary energy, transport, fugitive emissions, industrial processes and waste sectors, and all six greenhouse gases under the Kyoto Protocol.

1.6 An entity may incur obligations, including liability, for:

- direct 'scope 1' emissions from a facility
- potential emissions from fossil fuels that it imports, produces or supplies
- emissions from synthetic greenhouse gases that it imports, manufactures or supplies.

1.7 Emissions thresholds are used to define which facilities will be included in the Scheme. All direct emissions from a facility will count toward the facility-level threshold; however, entities may not be required to surrender emissions units (see Chapter 2) for all their direct emissions.

1.8 This is because the obligation for emissions from the combustion of most fuels will be placed on importers, producers or suppliers rather than the direct emitter. Placing liability on these entities means fewer entities will be liable under the Scheme, which reduces the compliance burden for entities.

1.9 For liquid petroleum fuels, liability will apply to the same entities that incur customs duty and excise duty. For most other fossil fuels the entities that first supply those fuels in Australia will be liable. Importers, producers and suppliers are specifically made liable in the draft provisions, and there will not be any emissions threshold for these entities.

1.10 Scheme obligations for synthetic greenhouse gas emissions will apply to entities that import or manufacture synthetic greenhouse gases with a carbon dioxide equivalence of 25,000 tonnes or more.

1.11 The *National Greenhouse and Energy Reporting Act 2007* provides the basis for reporting emissions under the Scheme, including coverage of sources and substances, and measurement of emissions. This approach streamlines emissions reporting and reduces the administrative burden on liable entities, many of which will already be reporting under that Act. Consequential amendments to that Act are included in the draft Carbon Pollution Reduction Scheme (Consequential Amendments) Bill 2009 (the consequential amendments bill) and described in a separate commentary.

Summary of new law

Key concepts

1.12 Key concepts and definitions relating to this chapter are explained in the detailed explanation of new law below. The draft bill includes a simplified outline of Part 3 ***[Part 3, Division 1, clause 16].***

Liable entities

1.13 In broad terms, a person can be liable under the Scheme if the person:

- is responsible for greenhouse gases emitted directly from a facility;
- imports, produces or supplies certain upstream fuels; or
- imports, manufactures or supplies synthetic greenhouse gas.

1.14 Significant aspects of Part 3 are:

- Division 2 of Part 3 outlines liability for greenhouse gases emitted from a facility (direct emissions)
  - Subdivision A relates to emissions from fuel combustion, industrial process and fugitive emissions, and emissions from waste sources at non-landfill facilities.
  - Subdivision B deals with emissions from landfill facilities.
- Divisions 3 and 4 of Part 3 outline liability for emissions that are not emitted from a facility
  - Division 3 deals with synthetic greenhouse gases.
  - Division 4 deals with liability for emissions from certain fuels, known as 'eligible upstream fuels'.

Direct emitters of greenhouse gases (other than landfill facilities)

1.15 In broad terms, Scheme obligations for greenhouse gas emissions apply to operators of facilities (other than landfill facilities) that have direct greenhouse gases emissions of 25 000 tonnes of 'carbon dioxide equivalence' (CO_2-e) a year or more.

1.16 Scheme obligations may be transferred from the operator of a facility to another person in some circumstances.

1.17 All scope 1 emissions that are covered by the Scheme will be covered for a facility (other than a landfill facility). This will include emissions from an ancillary solid waste disposal source that forms part of the facility.

1.18 Under the direct emitter provisions for facilities other than landfill facilities, liability does not apply to:

- facilities with emissions below 25 000 tonnes of CO_2-e a year

or

- in certain circumstances to avoid double-counting, emissions from the combustion of certain fuels.

Direct emitters of greenhouse gases - landfill facilities

1.19 Generally, entities with operational control over a landfill facility that has emissions of 25,000 tonnes of CO_2-e or more a year will be liable under the Scheme. However, if a landfill facility is within a prescribed distance of another landfill facility that accepts similar classifications of waste, the threshold is 10,000 tonnes of CO_2-e.

1.20 All scope 1 emissions covered by the Scheme will be covered for a landfill facility.

1.21 Under the direct emitter provisions for landfill facilities, scheme obligations do not apply to:

- facilities with emissions below these thresholds
- landfill facilities that have not accepted waste since 1 July 2008
- emissions attributable to 'legacy waste' for the period to 1 July 2018

or

- in certain circumstances to avoid double-counting, emissions that are attributable to the combustion of certain fuels.

Importers, manufacturers, suppliers and re-suppliers of eligible upstream fuels

1.22 In general terms, liability for emissions from the combustion of eligible upstream fuels is imposed on a person who:

- imports or produces the fuel
- supplies the fuel to another entity

or

- applies the fuel to their own use.

1.23 In certain circumstances liability for emissions from upstream fuels may be passed from the supplier to a customer. This occurs when a customer quotes an obligation transfer number (OTN) to a supplier for the fuel.

1.24 The customer would be liable for the potential emissions from the fuel if they re-supplied the fuel to another person who did not quote their OTN.

1.25 If the customer combusted the fuel, then the customer would be liable for the greenhouse gas emissions from its own use of the fuel.

Import, manufacture and re-supply of synthetic greenhouse gases

1.26 Liability for emissions from downstream use of synthetic greenhouse gases is imposed on:

- importers and manufacturers of synthetic greenhouse gas with emissions of 25,000 tonnes of CO_2-e or more per year
- in certain circumstances, people who re-supply those gases.

1.27 Scheme liability for synthetic greenhouse gas emissions do not apply to:

- synthetic greenhouse gases that are exported
- synthetic greenhouse gases that are imported on board ships or aircraft where the gas is used to meet the reasonable servicing requirements of that ship or aircraft
- synthetic greenhouse gases imported in products that contain a synthetic greenhouse gas because the gas was used to manufacture that product

or

- synthetic greenhouse gases that are produced by recycling.

Obligation transfer numbers

1.28 Division 5 establishes OTNs. This is a mechanism designed to manage Scheme obligations between upstream fuel suppliers and direct emitters and avoid double-counting of emissions and gaps in coverage. It allows Scheme obligations to be transferred from upstream suppliers of fuels and synthetic greenhouse gases to intermediate suppliers and end users.

1.29 The valid quotation of an OTN to an upstream supplier relieves the supplier of liability for that supply and transfers a potential liability to the entity that quotes the OTN.

1.30 OTNs have a number of roles in transferring liability:

- OTNs allow certain entities to assume liability for emissions from the combustion of particular fuels.
- OTNs allow entities to assume liability, if any arises, for certain fuels or synthetic greenhouse gases that are sequestered into a product (that is, used as feedstock) or used in a way that results in emissions that do not count towards Australia's national inventory (such as export).
- In the case of natural gas and liquid petroleum gas, OTNs move the bulk of scheme obligations from upstream suppliers (producers or importers) to re-suppliers who have access to accurate customer usage information.
- OTNs prevent double counting where entities transform one type of fuel into another type of fuel (for example, from coal to coke).

Liability transfer certificates

1.31 Division 6 outlines the two circumstances in which the liability for a particular facility can be transferred from one entity to another using a liability transfer certificate.

1.32 The first circumstance applies to corporations only. A member of a controlling corporation's group may take on liability in relation to a particular facility in certain circumstances. If the member fails to meet its obligations, liability will revert back to the controlling corporation.

1.33 The second circumstance applies when an entity that has financial control over a facility may have greater influence over emissions than the operator. In line with the object of the Scheme – to reduce emissions – the entity that has financial control may take on liability in certain circumstances. If more than one entity has financial control, it is intended that the entity with the greatest financial control would be permitted to apply for a liability transfer certificate.

1.34 All reporting obligations under the *National Greenhouse and Energy Reporting Act 2007*, including reporting of greenhouse gas emissions, energy production and energy consumption data, in relation to the facility for which a liability transfer certificate is issued will be transferred to the holder of the certificate.

Detailed explanation of new law

Key concepts

1.35 Key concepts and definitions referred to throughout this chapter are explained in this section.

1.36 Several of these concepts are defined in the draft bill as having the same meaning as in the *National Greenhouse and Energy Reporting Act 2007*. In a number of cases the definitions in that Act will be amended or introduced by the draft consequential amendments bill.

Greenhouse gas

1.37 'Greenhouse gas' will have the same meaning as in the *National Greenhouse and Energy Reporting Act 2007*. ***[Part 1, clause 5, definition of 'greenhouse gas']*** This definition will be amended by the draft consequential amendments bill to provide for additional gases to be included through regulations. (See the consequential amendments bill, Schedule 1, Part 2, item 146) This will allow for the inclusion of any additional greenhouse gas which is recognised in a post-2012 international agreement.

1.38 The amended definition will cover

- carbon dioxide
- methane
- nitrous oxide
- a synthetic greenhouse gas
- a prescribed greenhouse gas.

1.39 The following gases are synthetic greenhouse gases:

- sulphur hexafluoride
- a hydrofluorocarbon of a kind specified in the *National Greenhouse and Energy Reporting Act 2007*
- a perfluorocarbon of a kind specified in the *National Greenhouse and Energy Reporting Act 2007*.

Carbon dioxide equivalence

1.40 Carbon dioxide equivalence (CO_2-e) has the same meaning as in the *National Greenhouse and Energy Reporting Act 2007*. ***[Part 1, clause 5, definition of 'carbon dioxide equivalence']*** That is, the CO_2-e of an amount of greenhouse gas (metric weight) means the amount of the gas multiplied by a value specified in the *National Greenhouse and Energy Reporting Regulations 2008* in relation to that kind of greenhouse gas. This value is the internationally accepted global warming potential for that gas.

1.41 This definition will be amended by the draft consequential amendments bill to provide for calculating:

- the carbon dioxide equivalence of an amount of greenhouse gas
- the carbon dioxide equivalence of an amount of potential greenhouse gas emissions embodied in an amount of an eligible upstream fuel.

(See the consequential amendments bill, Schedule 1, Part 2, items 112, 146)

Potential greenhouse gas emissions embodied in an amount of eligible upstream fuel

1.42 Potential greenhouse gas emissions embodied in an amount of an eligible upstream fuel will have the same meaning as in the *National Greenhouse and Energy Reporting Act 2007*. ***[Part 1, clause 5, definition of 'potential greenhouse gas emissions']*** The draft consequential amendments bill defines this concept. (See the consequential amendments bill, Schedule 1, Part 2, items 135, 146)

1.43 In broad terms, the potential greenhouse gas emissions embodied in an amount of an eligible upstream fuel means the amount(s) of the greenhouse gas(es) that would be released into the atmosphere as a result of the combustion of the fuel.

Facility and landfill facility

1.44 Facility is given the same meaning as in the *National Greenhouse and Energy Reporting Act 2007*. ***[Part 1, clause 5, definition of 'facility']*** Whether an entity meets a facility threshold, as outlined below, is the key determinant for liability if an entity has scope 1 (direct) emissions.

1.45 A 'landfill facility' is defined separately in the draft bill. The term 'landfill facility is defined to mean a facility for the disposal of solid

waste as landfill, and includes a facility that is closed for the acceptance of waste. ***[Part 1, clause 5, definition of 'landfill facility']*** The definitions lead to a distinction between facilities the sole purpose of which is the disposal of waste and facilities where other activities that produce waste are conducted. For example a mine may have its own on-site waste. Specific provisions outlined below relate only to landfill facilities.

Operational control

1.46 A corporation is considered to have operational control over a facility if it has authority to introduce and implement operating, health and safety, and environmental policies. In general, only one corporation can have operational control over a facility at any time.

1.47 If there is uncertainty about which corporation has operational control over a facility, the corporation deemed to have operational control will be the one with the greatest authority to introduce and implement operating and environmental policies.

1.48 Where there is uncertainty in determining 'greatest authority', the decision rule is limited to operating and environmental policies; it does not include health and safety policies.

1.49 A new provision has been included for circumstances where more than one entity shares operational control in equal parts. This is discussed in more detail below in the section on operational control.

Emission of greenhouse gas from the operation of a facility

1.50 An emission of greenhouse gas from the operation of a facility is defined as a scope 1 emission of greenhouse gas, where:

- the greenhouse gas is released into the atmosphere as a direct result of the operation of the facility
- regulations made for the purposes of paragraph 10(2A)(a) of the *National Greenhouse and Energy Reporting Act 2007* declare that the emission is a scope 1 emission covered by the Scheme. ***[Part 3, Division 2, clause 24]***

1.51 The draft consequential amendments bill will amend the *National Greenhouse and Energy Reporting Act 2007* to require that its regulations specify scope 1 emissions that are covered by the Scheme. (See the consequential amendments bill, Schedule 1, Part 2, item 159)

1.52 Scope 2 emissions, such as those relating to electricity use, are not included in the definition of a facility's emissions. Scope 3 emissions are also not covered by the Scheme.

1.53 The broad categories of sources that will be declared in the *National Greenhouse and Reporting Regulations 2008* as scope 1 emission covered by the Scheme are:

- fugitive emissions
- industrial process emissions
- emissions from a waste source
- emissions from the combustion of energy sources.

1.54 The key sources that will be excluded from direct emitter liability are:

- agriculture sources
- forestry sources
- fugitive emissions from decommissioned underground coal mines
- emissions of synthetic greenhouse gases from the source "use of commercial air conditioning etc." as currently defined under the *National Greenhouse and Energy Reporting Regulations 2008*
- emissions from the combustion of biomass.

Eligible upstream fuel

1.55 Eligible upstream fuels are fuels for which an upstream point of liability is imposed. Eligible upstream fuels are:

- liquid petroleum fuel
- liquid petroleum gas
- black coal
- brown coal
- coking coal

- brown coal briquettes
- coke oven coke
- coal-based char
- natural gas that is distributed or transmitted in a pipeline
- coal seam methane that is captured for combustion
- coal mine waste gas that is captured for combustion
- ethane
- town gas
- liquefied natural gas
- compressed natural gas
- syngas
- a fuel specified in the regulations.

[Part 1, clause 5, definition of 'eligible upstream fuels']

1.56 Liquid petroleum fuels are defined by reference to the *Excise Tariff Act 1921*. ***[Part 1, clause 5, definition of 'liquid petroleum fuels']*** In broad terms, liquid petroleum fuels are excisable goods classified to items 10 and 15 of the Schedule to the *Excise Tariff Act 1921*.

1.57 Eligible upstream fuels (other than liquid petroleum fuels) are defined by reference to the *National Greenhouse and Energy Reporting Regulations 2008* which will be amended to define fuel types not currently defined in these regulations, such as coal-based char and syngas.

1.58 The purpose of the regulation-making power is to enable an upstream point of liability to be applied wherever emissions from other fossil-based fuels, including new fuels, can be efficiently covered upstream.

Provisional emissions number

1.59 A provisional emissions number forms part of the calculation of an entity's liability under the Scheme under Part 5 of the draft bill. (This calculation is explained in Chapter 8.)

1.60 A provisional emissions number will arise for:

- emissions from a facility
- potential emissions from the supply of an eligible upstream fuel or synthetic greenhouse gas
- an entity's own use of an eligible upstream fuel.

1.61 The value of the provisional emissions number in each situation is discussed in the detailed explanation of new law. In broad terms, it is equal to the amount of the particular emissions, in CO_2-e, adjusted by any relevant exclusions or other provisions.

Supply

1.62 Supply means supply, including re-supply, by way of sale, exchange or gift. ***[Part 1, clause 5, definition of 'supply']***

1.63 When supply occurs:

- For substances other than natural gas in a pipeline, supply occurs when the substance is physically delivered.
- For natural gas in a pipeline, in most cases, supply occurs when the gas passes a metering point ascertained in accordance with the regulations. If there is no metering point, supply occurs when the gas passes a point ascertained in accordance with the regulations.

[Part 1, clause 6]

Obligation transfer number

1.64 An OTN enables the transfer of Scheme obligations from upstream suppliers to intermediate suppliers and end users of fuels and synthetic greenhouse gases. ***[Part 3, Division 5]***

1.65 The valid quotation of an OTN to an upstream supplier relieves the supplier of liability to surrender emissions units for that supply and transfers a potential liability to the person that quotes the OTN. ***[Part 3, Division 3] [Part 3, Division 4]***

1.66 The Authority must only issue an OTN to persons that are likely to be permitted or required by the draft bill to quote an OTN. The circumstances under which a person is permitted or required to quote an OTN are specified in the draft bill. ***[Part 3, Division 5]***

Person

1.67 The coverage of legal entities is given effect through the definition of a 'person'. The Scheme may apply obligations to any legal entity. Legal entities are captured as broadly as possible, ranging from an individual to a corporation, a trust (a trustee or trust estate), a body corporate, and Commonwealth, State, Territory and local Governments – these are examples only and this is not intended as an exhaustive list. ***[Part 1, clause 5, definition of 'person']***

1.68 Government bodies will be bound by the draft bill. Key financial penalties, such as penalties for failing to surrender sufficient emission units, apply to government bodies. However, in line with usual practice this clause ensures that the Crown is not subject to a pecuniary or criminal penalty. ***[Part 1, clause 9]***

1.69 These legal entities may be liable under the Scheme if they meet the criteria for liable entities under Part 3 of the draft bill.

1.70 A definition of a 'non-group entity' is included to identify entities that are not members of a controlling corporation's group - that is not a constitutional corporation ***[Part 1, clause 5, definition of 'non-group entity']***. (See the consequential amendments bill, Schedule 1, Part 2, item 129)

Liable entities – general rules for all facilities

1.71 This section describes general rules that apply to all facilities; that is, landfill facilities and non-landfill facilities. Specific rules for landfill facilities including those relating to closed landfill facilities, past waste streams (legacy waste) and additional thresholds for landfill facilities are described separately in the section on landfill facilities below.

Thresholds for covered facilities

1.72 Entities will only be liable for covered facilities. In broad terms, a facility is covered by the Scheme if emissions of greenhouse gases from its operation are 25 000 tonnes of CO_2-e or more a year. ***[Part 3, Division 2, clauses 17-18]***

1.73 If, during a relevant financial year an entity has operational control over a small facility the emissions from that facility do not form part of an entity's liability – that is, the facility is not covered by the Scheme for that financial year. In most cases a small facility is a facility that emits less than 25,000 tonnes of CO_2-e during a financial year. ***[Part 3, Division 2, clause 17(4)-(5)], [Part 3, Division 2, clause 18(4)-(5)], [Part 3, Division 2,***

clause 19(4)-(5)] [Part 3, Division 2, clause 20(4)-(5)], [Part 3, Division 2, clause 21(4)-(5)], [Part 3, Division 2, clause 22(4)-(5)]

[Part 3, Division 2, clause 17(1), 17(3)-(5), 18(1), 18(3)-(5), 19(1), 19(3)-(5), 20(1), 20(3)-(5), 21(1), 21(3)-(5), 22(1), 22(3)-(5)]

Pro-rata thresholds

1.74 Pro-rata emissions thresholds will apply in the following circumstances:

- a facility is under the operational control of a member of a controlling corporation's group for part of a year
- a facility is under the operational control of a non-group entity for part of a year

or

- an entity is the holder of a liability transfer certificate for part of a year.

1.75 Pro-rata thresholds are calculated using a specified formula. ***[Part 3, Division 2, clause 17(5)] [Part 3, Division 2, clause 18(5)] [Part 3, Division 2, clause 19(5)] [Part 3, Division 2, clause 20(5)] [Part 3, Division 2, clause 21(5)] [Part 3, Division 2, clause 22(5)]***

1.76 The pro-rata formula takes the threshold for a covered facility and multiplies that threshold by the number of control days for a facility, or the number of certificate days in the case of the holder of a liability transfer certificate, divided by the number of days in the year.

1.77 Control days are the days in the financial year, where this is less than the full year, that a facility was under the operational control of one or more members of a controlling corporation's group. ***[Part 3, Division 2, clauses 17-18]***

1.78 Certificate days are the days in the financial year, where this is less than the full year, that a person was the holder of a liability transfer certificate for a facility. ***[Part 3, Division 2, clause 19]***

Example 1.1 Pro rata threshold

If a non-group entity had operational control of a facility for 100 days of the year, the threshold for that facility would be worked out using the formula:

25,000 × (100 control days ÷ 365) = 6849 tonnes of CO_2-e

If the emissions from that facility are 6849 tonnes CO_2-e or more during the 100 control days then those emissions will count towards an entity's provisional emissions number as outlined above.

1.79 The pro-rata threshold is applied in recognition that there will always be an entity that has operational control of a facility, but that liability for a facility may change hands when an entity with operational control changes or an entity takes on a liability transfer certificate for part of a year and not a whole year. The pro-rata threshold ensures that facilities that would reach the 25 000 tonnes of CO_2-e threshold during an entire financial year continue to be covered under the Scheme. This maintains consistent coverage under the Scheme and prevents entities from avoiding thresholds, deliberately or otherwise, by changes in operational control or the issue of a liability transfer certificate.

Anti-avoidance

1.80 Provisions which address schemes entered into with the substantial purpose of obtaining the advantage of the thresholds are described in Chapter 9 of this commentary. ***[Part 3, Division 2, clauses 23 and 30]*** In brief, the benefit of the threshold provision may be lost.

Sources of emissions

1.81 Regulations made for the purposes of paragraph 10(2A)(a) of the *National Greenhouse and Energy Reporting Act 2007* will declare sources of scope 1 emissions that will be covered by the Scheme. ***[Part 3, Division 2, clause 24]*** This will be provided for in amendments to the *National Greenhouse and Energy Reporting Act 2007.* (See the consequential amendments bill, Schedule 1, Part 2, item 159.) Emissions covered by the Scheme are discussed in more detail in the key concepts section of this chapter.

1.82 In particular, for facilities other than landfill facilities, emissions from a solid waste disposal source that forms part of the facility are covered.

1.83 All sources of emissions covered by the Scheme will contribute towards thresholds for all facilities.

Provisional emissions number

1.84 The provisional emissions number for a person that is liable in respect of a facility will be the amount of greenhouse gases emitted from the facility's operation, in CO2-e, provided this exceeds a relevant threshold. ***[Part 3, Division 2]***

Avoidance of double counting

1.85 To avoid double counting of emissions, certain emissions are not counted towards an entity's provisional emissions number. Specifically, scheme obligations do not apply:

- in the case of the controlling corporation of a group, where a person holds a liability transfer certificate in relation to the facility ***[Part 3, Division 2, clauses 17(6) and 20(8)]***

- where an amount of greenhouse gas emitted from the facility is attributable to the combustion of eligible upstream fuel that was supplied to a person with operational control over a facility and the person did not quote the entity's OTN in relation to the supply ***[Part 3, Division 2, clauses 17(7)-(8,) 18(6)-(7), 19(6)-(7), 20(9)-(10), 21(9)-(10) and 22(8)-(9)]***

- where an amount of greenhouse gas emitted from the facility is attributable to the combustion of liquid petroleum fuel for which there is already a liability imposed under the import or production provisions for these fuels ***[Part 3, Division 2, clauses 17(9)-(10), 18(8)-(9), 19(8)-(9), 20(11)-(12), 21(11)-(12) and 22(10)-(11)]***

1.86 Scheme liability for emissions attributable to eligible upstream fuel supplied without OTN quotation will be covered by upstream suppliers.

1.87 Where a person imports, manufactures or produces petroleum fuel and then uses that fuel itself a liability may arise under the provisions relating to eligible upstream fuels. Where this is the case, a liability does not arise for that same fuel under the direct emitter provisions.

Example 1.2 Avoidance of double counting

Company A has operational control of a black coal mine. During a particular financial year fugitive emissions of 23 000 tonnes of CO_2-e are emitted from the mine. A further 3 000 tonnes of CO_2-e are emitted from the combustion of diesel in equipment at the mine. Company A does not quote an OTN for the supply of the diesel.

Company A is a liable entity under the direct emitter provisions because total emissions from the mine are 26 000 tonnes of CO_2-e.

Company A is only liable for the fugitive emissions of 23 000 tonnes of CO_2-e. The upstream supplier of the diesel is liable for the emissions from combustion of the diesel.

Measurement of greenhouse gas emitted from facilities

1.88 Greenhouse gas emitted from the operation of a facility is a defined concept ***[Part 3, Division 2, clause 24]*** It is to be measured using methods to be determined under subsection 10(3) of the *National Greenhouse and Energy Reporting Act 2007*, or methods which meet criteria under that subsection, where the use of those methods satisfies any conditions specified under that subsection. ***[Part 3, Division 2, clause 25]***

1.89 The draft consequential amendments bill provides for subsection 10(3) of the *National Greenhouse and Energy Reporting Act 2007* to allow the Minister to determine the methods and criteria for methods, by which amounts of emissions are to be measured. A single determination will apply under the Carbon Pollution Reduction Scheme and the *National Greenhouse and Energy Reporting Act 2007.* (See the consequential amendments bill, Schedule 1, Part 2, item 160-162)

Operational control

General

1.90 'Operational control' is used to allocate emissions obligations for a covered facility. The operational control approach is adopted for the Scheme as it places obligations on the entity that has the greatest ability to introduce and implement operational and environmental policies for a covered facility. In addition many entities have already begun organising emission reporting systems around the operational control approach as defined in the *National Greenhouse and Reporting Act 2007*. Exceptions relating to liability transfer certificates are outlined below.

1.91 Operational control has the same meaning as in the *National Greenhouse and Reporting Act 2007*. ***[Part 1, clause 5, definition of 'operational control']*** This definition will be amended as discussed in the remainder of this section. (See the consequential amendments bill, Schedule 1, Part 2, items 131 and 163-172)

1.92 Any person may have operational control over a facility. The draft consequential amendments bill broadens the range of entities that can have operational control in the *National Greenhouse and Reporting Act 2007* from a member of a controlling corporation's group to a person. (See the consequential amendments bill, Schedule 1, Part 2, item 163-170)

1.93 In addition, the entities that the Authority may *declare* as having operational control will be expanded to include any person. This is provided for by amendments to the *National Greenhouse and Energy Reporting Act 2007*. (See the consequential amendments bill, Schedule 1, Part 2, items 190-191 and 193)

1.94 The Government intends that liability for a facility will always be attributable to a single person. This streamlines compliance and enforcement under the Scheme and assists in maintaining Scheme coverage and integrity by ensuring responsibilities for facility emissions are clearly identified.

Circumstances where authority is shared equally amongst entities

1.95 In many cases, if there is uncertainty about which corporation has operational control over a facility, the corporation deemed to have operational control will be the one with the greatest authority to introduce and implement operating and environmental policies. (See the consequential amendments bill, Schedule 1, Part 2, item 172)

1.96 However, there may be instances where entities have equal authority to implement operational and environmental policies over a facility, for example in the case of a partnership, a joint venture or a trust. Proposed amendments to the *National Greenhouse and Reporting Act 2007* to insert new sections 11B and 11C will deal with these circumstances. (See the consequential amendments bill, Schedule 1, Part 2, item 172) In these instances the Authority will still have the ability to make a declaration regarding operational control.

1.97 If the Authority has not made a declaration, then those persons with equal authority will be required to nominate one of them to be the nominated person for that facility. Nomination has the effect of deeming that entity to have operational control and therefore obligations and liability under the Scheme and the *National Greenhouse and Energy Reporting Act 2007*. Nominations must be made by the 31st August following the relevant financial year.

1.98 If the entities do not nominate, they will be subject to a penalty. In addition, liability will be apportioned equally among the entities that have equal authority. For example, if there are two entities, each will be responsible for fifty percent of total liability. If there are four entities each will be responsible for twenty-five percent of total liability. Each entity will also have reporting obligations in relation to that facility; however, it is intended that a joint report could satisfy their reporting requirements.

1.99 The penalty discussed above is aimed at encouraging the nomination of a single liable entity under the Scheme. The application of equal liability applying in the absence of nomination is important for the integrity of the Scheme as it ensures that there is no gap in liability at any time.

1.100 Note that equally shared authority is distinct from shared financial control under a partnership, joint venture or trust, which is

discussed below under liability transfer certificates. The provisions relating to operational control in the draft bill do not reflect the policy outlined above on shared liability. This will be addressed in the final legislation.

Liability for a facility applies to controlling corporations of a corporate group, non-group entities and holders of a liability transfer certificate

1.101 Liable entities, in relation to direct emissions from a covered facility, can be a controlling corporation of a group, a non-group entity or a holder of a liability transfer certificate. There will only be one liable entity at any point in time. 'Controlling corporation' and 'non-group entity' will have the same meaning as in *National Greenhouse and Reporting Act 2007*. The draft consequential amendments bill will insert a definition of 'non-group entity' into the *National Greenhouse and Reporting Act 2007*. (See the consequential amendments bill, Schedule 1, Part 2, item 129)

Controlling corporations and corporate groups

1.102 The controlling corporation of a group will be the liable entity for facilities that are under the operational control of a member of its group (this includes the controlling corporation itself). ***[Part 3, Division 2, clauses 17, 20]***

1.103 This is consistent with the *National Greenhouse and Reporting Act 2007*, which imposes reporting obligations on controlling corporations of a corporate group, where a controlling corporation is generally the corporation at the top of the corporate hierarchy. Corporate grouping in this way also provides greater surety for the Scheme as the controlling corporation is likely to have greater access to funds and will therefore have a greater ability to meet its Scheme liability than an individual corporation with a single facility might otherwise have.

1.104 A controlling corporation's group will consist of the controlling corporation and its subsidiaries, if any. Subsidiary has the meaning given by section 46 of the *Corporations Act 2001*. To avoid doubt, a controlling corporation's group may consist of the controlling corporation alone. The draft consequential amendments bill provides for this by amending the *National Greenhouse and Reporting Act 2007*, as discussed in Chapter 1 of the commentary to the draft consequential amendments bill.

1.105 A non-group entity that has operational control over a covered facility is the liable entity under the draft bill in relation to that facility. ***[Part 3, Division 2, clause 18 and 21]***

1.106 An entity that is the holder of a liability transfer certificate for a covered facility is the liable entity under the draft bill in relation to that facility. ***[Part 3, Division 2, clauses 19 and 22]***

1.107 Where a member of a controlling corporation's group takes on liability through a liability transfer certificate under Part 3, Division 6, Subdivision A, the controlling corporation will not have liability for that facility. ***[Part 3, Division 2, clause 17(6)] [Part 3, Division 2, clause 20(8)]*** However, the controlling corporation must give its consent to the transfer and provides a statutory guarantee for the payment of the penalty for a unit shortfall and any late payment penalty for that member. ***[Part 6, Division 4, clause 138]***

1.108 Where liability has been transferred to a company with financial control of a facility, the facility is taken not to be under the operational control of its operator and the operator's controlling corporation (the transferor of liability) will therefore not have obligations or liability for the facility. ***[Part 3, Division 2, clauses 17(6) and clause 20(8)]***

1.109 Note that the transferors of liability will also not have reporting obligations under the Scheme as these obligations are transferred to the holder of the liability transfer certificate. The provisions relating to reporting obligations in the draft bill do not reflect this policy. This will be addressed in the final legislation.

1.110 Liability transfer certificates are discussed in more detail in a separate section below.

Liable entities – landfill facilities

1.111 This section details specific provisions that relate to landfill facilities only. These provisions do not apply to non-landfill facilities, even though a non-landfill facility may have emissions from solid waste disposal. Non-landfill facilities that have emissions from solid waste disposal, as in the example of a mine that has on-site waste, will still be required to report those emissions as outlined in the *National Greenhouse and Energy Reporting (Measurement) Determination 2008.*

1.112 General rules described above relating to facilities also apply to landfill facilities.

1.113 For the purposes of landfill facilities, emissions from a solid waste disposal source are categorised into two components. The first component is emissions from past waste, or 'legacy emissions', generated from waste deposited prior to 1 July 2008. The second component is emissions from new waste; that is, emissions from waste deposited from 1 July 2008 onwards.

Thresholds for covered landfill facilities

1.114 Thresholds for landfill facilities include all scope 1 emissions from the facility; that is, all scope 1 emissions that are covered under the Scheme including emissions from legacy waste and emissions from new waste.

1.115 Generally, landfill facilities which have emissions of 25,000 tonnes or more of carbon dioxide equivalence per year will be liable for these emissions under the Scheme. ***[Part 3, Division 2, clauses 20-22]*** This will be determined over a financial year, or on a pro-rata basis for the number of control days for which a landfill facility was under the operational control of a controlling corporation's group.

1.116 If a landfill facility is within a certain distance of another landfill facility the threshold is lowered to 10,000 tonnes or more of carbon dioxide equivalence. ***[Part 3, Division 2, clause 20(13)], [Part 3, Division 2, clause 21(13)], [Part 3, Division 2, clause 22(12)]*** This distance will be specified in the regulations. It is intended that this would apply to competing landfills accepting the same classification of waste. Provisions relating to this requirement are yet to be drafted.

1.117 A lower threshold is used in these circumstances to prevent the translocation of waste from a landfill facility that meets or exceeds a threshold of 25,000 tonnes of carbon dioxide equivalence to a landfill facility that does not meet this threshold.

1.118 If a landfill facility closes, and its threshold number for the last financial year that it was open was 10,000 tonnes of carbon dioxide equivalence, then its threshold for the next 10 years is 10,000 tonnes of carbon dioxide equivalence.

[Part 3, Division 2, clause 20(4-5), (13)], [Part 3, Division 2, clause 21(4-5), (13)], [Part 3, Division 2, clause 22(4-5), (12)]

Closed landfill facilities

1.119 Emissions from landfill facilities that closed prior to 30 June 2008 will not be covered. That is, if a landfill facility has not accepted any waste between 1 July 2008 and the end of the last day of the relevant financial year, emissions from this facility will not be covered. ***[Part 3, Division 2, clause 20(6)], [Part 3, Division 2, clause 21(6)], [Part 3, Division 2, clause 22(6)]***

1.120 Liability for emissions from landfill facilities that close after 30 June 2008 will remain with the entity which had operational control of the facility at closure. In the event that operational control changes after

the facility is closed, obligations would transfer to the new operator. Provisions relating to this requirement are yet to be drafted.

Legacy emissions

1.121 Emissions from legacy waste are excluded from the Scheme until 2018 and are not included as part of a landfill facility's liability until then. Therefore, a landfill facility's liability until 2018 is annual total emissions minus annual legacy emissions. ***[Part 3, Division 2, clause 20(7)], [Part 3, Division 2, clause 21(7)], [Part 3, Division 2, clause 22(7)]***

1.122 Legacy waste emissions have been excluded from Scheme liabilities until 2018 because some operators will have difficulties passing on Scheme costs for emissions from past waste streams. By 2018, legacy emissions will fall substantially. Excluding them for this period will reduce the financial impact on landfill operators and give them time to assess other abatement opportunities.

1.123 The Scheme will allocate methane that is captured and combusted proportionally between legacy and new emissions. It is intended that this allocation will be given effect by an amendment to the *National Greenhouse and Energy (Measurement) Determination 2008*.

Example 1.3 Participation and liability for landfill facilities pre-1 July 2018

In 2012-13, emissions from a landfill facility under the operational control of Company C are 100,000 tonnes of CO_2-e. This is made up of 20,000 tonnes of new emissions and 80,000 tonnes of legacy emissions. Assuming the landfill facility is outside the specified distance (as prescribed in the Regulations) of another competing landfill facility, the following applies:

- The landfill facility is covered under the Scheme. The total emissions from the landfill facility (100,000 tonnes of CO_2-e per year) exceed the participation threshold of 25,000 tonnes of CO_2-e per year.

- Company C's liability is equal to the total from the landfill facility minus legacy emissions. Therefore, Company C would be liable for 20,000 tonnes of CO_2-e in 2012-13.

Example 1.4 Participation and liability for landfill facilities after 1 July 2018

In 2020, the landfill facility under the operational control of Company D emits 100,000 tonnes of CO_2-e. This is made up of 70,000 tonnes of new emissions and 30,000 tonnes of legacy emissions. Assuming the facility is outside the specified distance (as prescribed in

the Regulations) of another competing landfill facility, the following applies:

- The total emissions from the landfill facility (100,000 tonnes of CO_2-e per year) exceed the participation threshold of 25,000 tonnes of CO_2-e per year.

- Company D is liable for all waste emissions from the landfill facility, including legacy emissions. Therefore, Company D is liable for 100,000 tonnes of CO_2-e in 2010.

Example 1.5 Allocating captured and combusted methane

In 2012-13, Company E has operational control over a landfill facility. Gross emissions from that landfill facility (prior to accounting for methane flaring) are 120,000 tonnes of CO_2-e. This is made up of 30,000 tonnes of CO_2-e of new emissions and 90,000 tonnes of CO_2-e of legacy emissions.

The landfill facility flares an amount of methane that reduces its net emissions to 60,000 tonnes of CO_2-e. Assuming the landfill facility is outside the specified distance (as prescribed in the Regulations) of another competing landfill facility, the following applies:

- The landfill facility is covered under the Scheme, as the total (net) emissions from the landfill facility (60,000 tonnes of CO_2-e per year) exceed the participation threshold of 25,000 tonnes of CO_2-e per year.

- The reductions in emissions achieved through methane flaring are allocated proportionally between legacy emissions and new emissions. Therefore, net new emissions are 15,000 tonnes of CO_2-e and net legacy emissions are 45,000 tonnes of CO_2-e.

- Company C is liable for the net new emissions equal to 15,000 tonnes of CO_2-e.

Transfer of liability

1.124 The provisions governing liability transfer certificates under Part 3, Division 6, subdivision B will be expanded prior to introduction of the draft bill into the Parliament so that they apply in relation to landfill facilities.

Liable entities - importers, manufacturers, suppliers and re-suppliers of eligible upstream fuels

1.125 Part 2, Division 4 of the draft bill sets out the circumstances under which importers, manufacturers, suppliers and re-suppliers of eligible upstream fuels will be liable for the emissions from downstream users of these fuels.

General concepts

1.126 In order to achieve comprehensive and efficient coverage of emissions from the combustion of certain fuels, liability is imposed upstream on entities that supply these fuels. This may be an importer, producer or other supplier. Under the draft bill, fuels for which there is an upstream point of liability are known as 'eligible upstream fuels'. ***[Part 3, Division 4, clauses 31-32] [Part 3, Division 4, clauses 33, 35, 37 and 40]***

1.127 Entities that supply eligible upstream fuels will also be liable for any of that fuel that they use themselves, if it results in greenhouse gas emissions. The purpose of this provision is to ensure that all fuel handled by these suppliers is covered by the Scheme. ***[Part 3, Division 4, clauses 34, 36, 38 and 39]***

1.128 In certain circumstances liability for emissions from upstream fuels may be passed from the supplier to a customer. This occurs when a customer quotes an OTN to a supplier for the fuel.

1.129 In broad terms, where an OTN holder quotes their OTN to a supplier in relation to the supply of an amount of eligible upstream fuel the OTN holder assumes liability for this fuel; that is, a potential liability transfers from the supplier to the OTN holder.

1.130 If the OTN holder then re-supplies this fuel to another person who does not quote an OTN in relation to the supply, the OTN holder is liable for the potential greenhouse gas emissions embodied in the fuel. ***[Part 3, Division 4, clause 37]***

1.131 If the OTN holder applies this fuel to their own use the OTN holder is liable for the greenhouse gas emissions released from the own use of this fuel. Liability is imposed under either the direct emitter provisions or 'application to own use' provisions. ***[Part 3, Division 2] [Part 3, Division 4, clauses 38-39]***

1.132 Eligible upstream fuels include liquid petroleum fuels, coal and natural gas. Eligible upstream fuels are discussed in more detail in the key concepts/definitions section of this chapter.

1.133 Each amount of eligible upstream fuel has an amount of potential greenhouse gas emissions embodied in it - the amount of greenhouse gas or gases that would be released into the atmosphere as a result of the combustion of the fuel. The potential greenhouse gas emissions embodied in an amount of eligible upstream fuel is discussed in more detail in the key concepts/definitions section of this chapter.

1.134 Under amendments proposed to be made to the *National Greenhouse and Energy Reporting Act 2007* the potential greenhouse gas emissions embodied in an amount of eligible upstream fuel will be able to be calculated in two ways. (See the consequential amendments bill, Schedule 1, Part 2, item 146)

- Under the first method, known as the default method, the Minister may determine that the amount of a particular greenhouse gas that would be released into the atmosphere as a result of the combustion of an amount of eligible upstream fuel is taken, for the purposes of the Scheme, to be the amount of fuel multiplied by a value specified in the regulations in relation to that fuel.

- Alternatively, a person may elect to use a prescribed alternative method to ascertain the potential greenhouse gas emissions embodied in an amount of eligible upstream fuel. This involves, amongst other things, using a method specified in the determination which involves testing one or more samples of the fuel.

Liable entity - importers, producers and suppliers of liquid petroleum fuel

Application of provisions

1.135 The starting point for applying Scheme liability for liquid petroleum fuel is where:

- a person imports or manufactures / produces an amount of liquid petroleum fuel

- import duty or excise duty is or was payable by the person on that amount ***[Part 3, Division 4, clauses 31-32]***

1.136 This applies liability for liquid petroleum fuel at the top of the supply chain and aligns Scheme liability with fuel tax arrangements.

1.137 Scheme liability is not imposed where import duty or customs duty is or was payable by a person on an amount of fuel and:

- the duty was remitted, rebated or refunded in accordance with section 163 of the *Customs Act 1901* (the Customs Act) or section 178 of the *Excise Act 1901* (the Excise Act) or a drawback of duty was allowed under regulations made for the purposes of sections 168(1) and 79 of those Acts respectively

- the remission, rebate, refund or drawback was prescribed by regulations under the draft bill ***[Part 3, Division 4, clause 31(5)] [Part 3, Division 4, clause 32(5)]***

1.138 This is to ensure that scheme liability is not imposed in circumstances such as where excise duty or customs duty has been paid but that fuel is exported by the person or that fuel is returned to a warehouse or manufacturer.

1.139 Specific arrangements for the treatment of fuel emissions generated from the carriage of domestic cargo on ships engaged in an international voyage are not addressed in the draft bill. The Government is currently developing measures separate to the CPRS to address these emissions. There may be some interaction between these measures and the Scheme, and the Government will ensure that the measures are consistent and complementary.

Provisional emissions number

1.140 A person's provisional emissions number equals the potential greenhouse gas emissions embodied in the eligible upstream fuel for which the person has a liability to pay import or excise duty, minus any 'netted-out' number of the person. ***[Part 3, Division 4, clause 31(2)] [Part 3, Division 4, clause 32(2)].***

1.141 A person's 'netted-out' number refers to the potential greenhouse gases embodied in liquid petroleum fuel that the person supplied to another person who quoted an OTN in relation to that supply. ***[Part 3, Division 4, clause 31(4)] [Part 3, Division 4, clause 32(4)].***

1.142 This ensures that a person does not incur liability under the Scheme for the potential greenhouse gas emissions embodied in an amount of liquid petroleum fuel for which another person has assumed Scheme liability.

Liable entity - supply of eligible upstream fuel (other than liquid petroleum fuel)

Application of provision

1.143 The starting point for applying liability for eligible upstream fuels other than liquid petroleum fuels is the entity that first supplies an amount of these fuels to another person. That is, if a person (a supplier) supplies an amount of eligible upstream fuel (other than liquid petroleum fuel) to another person and that fuel was not supplied in Australia to the supplier, the supplier will be liable for the potential greenhouse gas emissions embodied in that fuel ***[Part 3, Division 4, clause 33]***.

Provisional emissions number

1.144 The provisional emissions number for a person that supplies eligible upstream fuel (other than liquid petroleum fuel) is equal to the potential greenhouse gas emissions embodied in fuel supplied to entities that do not quote an OTN. Fuel supplied to entities that quote an OTN does not incur liability for the supplier.

1.145 As outlined below, a supplier may pass on or reduce their liability by supplying the fuel to a person who quotes the person's OTN in relation to the supply. ***[Part 3, Division 4, clause 33]***

Liable entity – re-supply of eligible upstream fuel (including liquid petroleum fuel)

Application of provision

1.146 In broad terms, where an OTN holder quotes their OTN in relation to the supply of an amount of eligible upstream fuel the OTN holder assumes liability for this fuel. If the OTN holder then re-supplies this fuel to another person who does not quote the person's OTN in relation to the supply, the re-supplier is liable for the potential greenhouse gas emissions embodied in the fuel ***[Part 3, Division 4, clause 37]***.

Provisional emissions number

1.147 As with suppliers of eligible upstream fuel (other than liquid petroleum fuel), the provisional emissions number is equal to the potential greenhouse gas emissions embodied in fuel supplied to entities that do not quote an OTN.

1.148 In circumstances where the re-supplied fuel is packaged for use otherwise than by combustion, and other conditions specified in the

regulations are satisfied, the provisional emissions number is reduced by the potential greenhouse gases emissions embodied in the packaged fuel. ***[Part 3, Division 4, clause 37(4)]***

1.149 The purpose of this provision is to ensure that liability is not incurred in respect of fuels which are not combusted (i.e., fuels which are packaged – e.g., in a bottle for use as a solvent). This is broadly consistent with the arrangements under section 41.10(2) of the *Fuel Tax Act 2006* under which entities which package fuels are currently eligible to receive a fuel tax credit.

1.150 Fuel re-suppliers that export fuel supplied to them under an OTN will not be liable for any amount of fuel exported.

Example 1.6 Re-supplier and exporter of black coal

Company G is a re-supplier and exporter of black coal. Company G purchases coal from several coal mines and quote its OTN in the relation to each supply. The potential greenhouse gas emissions embodied in that coal have a carbon dioxide equivalence of 100 000 tonnes. Company G:

- exports half of this coal (50 000 tonnes of CO_2-e)
- re-supplies coal with potential emissions of 40 000 tonnes of CO_2-e to a large coal user who quotes an OTN in relation to the supply
- re-supplies the remaining coal, with potential emissions of 10 000 tonnes of CO_2-e, to a number of small coal users who do not quote an OTN.

Company G is:

- not liable for the emissions embodied in the export coal
- not liable for the emissions embodied in the coal supplied to the large user
- liable for 10 000 tonnes of CO_2-e for the coal re-supplied to the small coal users.

Example 1.7 Packer of fuel for use otherwise than by combustion

Company S is an OTN holder that packages a certain type of liquid petroleum fuel into small bottles and re-supplies this fuel for use as solvent. Company S is supplied fuel with potential greenhouse gas emissions of 10 tonnes of CO_2-e. Company S quotes its OTN in relation to this supply. Company S packages the full amount of fuel

into small bottles, and any conditions specified in the Regulations are satisfied:

- the 10 tonnes of CO_2-e will be netted out from Company S's liability for the relevant financial year
- Company S will have liability in respect of the 0 tonnes of CO_2-e of potential emissions.

1.151 OTNs are discussed in more detail below.

Liable entity – supply of transformed eligible upstream fuel

1.152 Some eligible upstream fuels can be transformed from one type of eligible upstream fuel into another type of eligible upstream fuel. If a fuel is the subject of a transformation process, the potential greenhouse gas emissions embodied in the new (transformed) fuel may a different from that in the pre-transformed fuel. For example, coke oven coke embodies a different amount of emissions than the coal from which it is produced.

Application of provision

1.153 In general terms, if an entity carries out a recognised transformation of a fuel, the entity will become a liable entity in respect of the supply of the transformed fuel where the recipient of the fuel does not quote the recipient's OTN in relation to the supply ***[Part 3, Division 4, clause 35]***.

1.154 To avoid double counting a person that carries out a recognised fuel transformation will be permitted to quote an OTN in respect of the supply of pre-transformed fuel ***[Part 3, Division 5, clause 59]***.

1.155 A list of recognised transformations is contained in ***[Part 1, clause 5, definition of 'recognised transformation']*** of the draft bill. The regulations may add to this list.

Provisional emissions number

1.156 The provisional emissions number for suppliers of transformed fuels is equal to the potential greenhouse gas emissions embodied in eligible upstream fuel supplied to entities that do not quote an OTN.

Example 1.8 Manufacturer of compressed natural gas

A company purchases natural gas and transforms it into compressed natural gas. The company quotes an OTN when purchasing the natural gas:

- the company assumes liability for the potential greenhouse gas emissions embodied in the natural gas
- the company will be liable for the potential greenhouse gas emissions embodied in any amount of compressed natural gas that it supplies to a person who does not quote an OTN in relation to the supply
- the company is not liable for the potential greenhouse gas emissions embodied in any amount of compressed natural gas supplied to a person who quoted the person's OTN in relation to the supply
- the company is liable for any emissions from the application to own use of the pre-transformed fuel or the transformed fuel. Application to own use is explained in the following section.

Liable entity –application of eligible upstream fuel to own use

Application of provision

1.157 A person may also be liable for greenhouse gas emissions released into the atmosphere as a result of the application to own use of an amount of eligible upstream fuel. ***[Part 3, Division 4, clauses 34, 36, and 38-39]*** These provisions only apply where amongst other things:

- eligible upstream fuel is applied to a person's own use
- greenhouse gases are emitted from the application to own use
- the emissions of greenhouse gases are not covered under one of the direct emitter provisions; that is, the emissions are not attributable to a covered facility.

1.158 It is likely that many upstream suppliers of eligible upstream fuels will be direct emitters. ***[Part 3, Division 2, clauses 17-19]*** Where this is the case, their application to own use of fuels will be covered under the direct emitter provisions (described above in 'Liable entities – general rules for all facilities' and 'Liable entities – landfill facilities'). To avoid double counting, entities that are liable entities under the direct emitter provisions are excluded from liability under this provision. ***[Part 3, Division 2, clause 34(1)]***

1.159 The provisions relating to own use of fuel by an OTN holder only apply where that use results in the release of greenhouse gas into the atmosphere. The intention of these provisions is to cover the combustion of fuels, and not the use of fuels which do not result in the release of greenhouse gas into the atmosphere, such as the use of fuels as feedstock. ***[Part 3, Division 4, clause 38(1)] [Part 3, Division 4, clause 39(1)]***

1.160 Application to own use provisions aim to ensure that emissions from combustion of eligible upstream fuels are covered at all points in the supply chain and not just imposed on covered facilities. This is particularly important in the case of OTN holders that are not large direct emitters.

Provisional emissions number

1.161 The provisional emissions number for a supplier or an OTN holder that applies an amount of transformed or untransformed eligible upstream fuel to their own use is equal to the potential greenhouse gas emissions from the combustion of that fuel. ***[Part 3, Division 4, clauses 34, 36, 38-39].***

1.162 If a particular use of an eligible upstream fuel does not result in the release of greenhouse gas into the atmosphere (such as feedstock), the use will not be covered by these provisions. However, if a portion of the fuel used results in the release of greenhouse gas into the atmosphere, that portion would be covered. ***[Part 3, Division 4, clauses 38-39]***.

Example 1.9 Feedstock user of natural gas

A person receives an amount of natural gas and quotes the person's OTN in relation to the supply. The person uses a portion of the natural gas as a feedstock in a plastic manufacturing process that completely sequesters the natural gas into the plastic. The person also uses a portion of the natural gas for heating purposes.

The person will not be liable for the potential greenhouse gas emissions embodied in the portion of gas purchased with an OTN which is used as a feedstock. However, the person will be liable for greenhouse gas emissions released from the portion of fuel combusted for heating purposes.

1.163 The reference for Example 1.9 is ***[Part 3, Division 4, clauses 38-39].***

Example 1.10 Manufacturer of coke oven coke

Company T specialises in manufacturing coke-oven-coke from black coal. During a financial year Company T:

- quotes an OTN for an annual supply of black coal that embodies potential greenhouse gas emissions of 100,000 tonnes of CO_2-e
- emits greenhouse gases of 20,000 tonnes of CO_2-e from the use of this coal to manufacture coke-oven-coke, but has no other emissions from the facility
- supplies coke-oven-coke to a number of small entities that do not quote an OTN – the potential greenhouse gas emissions embodied in this coke-oven coke is 20,000 tonnes of CO_2-e
- supplies coke-oven-coke to one large facility that quotes an OTN – the potential greenhouse gas emissions embodied in this coke-oven coke is 60,000 tonnes of CO_2-e.

Company T*:*

- is not liable under the direct emitter provisions, but is liable under the upstream supplier provisions for 20,000 tonnes of CO_2-e of emissions from their own use of black coal
- is liable for 20,000 tonnes of CO_2-e for the coke-oven coke it supplies to small entities that do not quote an OTN
- is not liable for 60,000 tonnes of CO_2-e for the coke-oven coke it supplies to the facility that quotes an OTN.

Liable entities –importers, manufacturers and re-suppliers of synthetic greenhouse gases

1.164 Part 2, Division 3 of the draft bill sets out the circumstances under which importers, manufacturers and re-suppliers of synthetic greenhouse gases – hydroflurocarbons (HFCs), perfluorocarbons (PFCs) and sulphur hexafluoride (SF6) - will be liable for the emissions from downstream users of these gases.

Liable entity - import or manufacture of synthetic greenhouse gas

Application of provisions

1.165 In general terms, liability will arise where, during a particular financial year, a person imports or manufactures an amount of synthetic greenhouse gas with a carbon dioxide equivalence of 25 000 tonnes or more. The threshold will be based on gross imports or manufacture ***[Part 3, Division 3, clauses 26, 27]***.

1.166 An amount of synthetic greenhouse gas imported or manufactured is not counted towards an entity's provisional emissions number if it is:

- exported ***[Part 3, Division 3, clause 26(7)-(8)], [Part 3, Division 3, clauses 27(7)-(8)]***
- imported on board ships or aircraft where the gas is used to meet the reasonable servicing requirements of that ship or aircraft ***[Part 3, Division 3, clause 26(6)]***
- imported in products that contain a synthetic greenhouse gas because the gas was used to manufacture that product ***[Part 3, Division 3, clause 26(5)]***
- produced by recycling. ***[Part 3, Division 3, clauses 27(5)-(6)]***

1.167 An amount of synthetic greenhouse gas imported or manufactured will not count towards a person's provisional emissions number where, during the relevant financial year, the total amount of synthetic greenhouse gases imported or manufactured by the person has a carbon dioxide equivalence of less than 25,000 tonnes. ***[Part 3, Division 3, clause 26(4)], [Part 3, Division 3, clauses 27(4)]***

1.168 Synthetic greenhouse gas in certain manufactured products will not count towards an importer's provisional emissions number. ***[Part 3, Division 3, clause 26(5)]*** The reason for excluding these gases from an importer's provisional emissions number is because it is difficult to consistently identify such products and estimate the amount of synthetic greenhouse gas they contain. The gases are imported in products that contain the gases only because the gas was used in the manufacturing process. Examples include domestic appliances that contain polyurethane foam insulation that contains residual amounts of synthetic greenhouse gases.

1.169 Synthetic greenhouse gases that are imported on board ships or aircraft that are exclusively for use in meeting the 'reasonable servicing requirements' of air-conditioning or refrigeration equipment during international journeys will also not count towards an importer's provisional emissions number. ***[Part 3, Division 3, clause 26(6)]*** This is to avoid imposing liability on emissions that do not count towards Australia's net national emissions.

1.170 A quantity of synthetic greenhouse gases produced by the recycling of substances containing synthetic greenhouse gases of that quantity will not count towards a manufacturer's provisional emissions number. ***[Part 3, Division 3, clause 27(5)]*** This provision is to avoid double

counting by ensuring that synthetic greenhouse gases that have incurred scheme obligations which are then recycled are not counted a second time.

Provisional emissions number

1.171 The provisional emissions number of an importer or manufacturer of synthetic greenhouse gas is equal to the total amount, in CO_2-e, of synthetic greenhouse gases imported or manufactured (where this is 25,000 tonnes or more), minus any 'netted-out' numbers of the person for the relevant financial year ***[Part 3, Division 3, clause 26(2)] [Part 3, Division 3, clauses 27(2)]***.

'Netted-out' numbers

1.172 Where an importer or manufacturer of a particular type of synthetic greenhouse gas also exports the same type of synthetic greenhouse gas, and the gas was not supplied to the importer or manufacturer in Australia, the importer's / manufacturer's 'netted-out' number refers to the amount of that type of synthetic greenhouse gas the person:

- exported (in tonnes of CO_2-e), where that amount is less than the amount the person imported or manufactured

or

- imported or manufactured (in tonnes of CO_2-e), where the amount the person exported is more than the amount they imported or manufactured. ***[Part 3, Division 3, clause 26(7)], [Part 3, Division 3, clause 27(7)]***

1.173 This prevents the provisional emissions number from having a negative value.

1.174 The purpose of this provision is to ensure that a person's liability is reduced by the carbon dioxide equivalence of the same type of synthetic greenhouse gas exported by the person. Exported synthetic greenhouse gases (including gases re-exported as "heels" in ISO tankers) will not count towards Scheme liabilities as these gases do not count towards Australia's national emissions. ***[Part 3, Division 3, clauses 26-27]***

Example 1.11 Manufacturer of synthetic greenhouse gas

The total amount of a particular synthetic greenhouse gas manufactured by a person has a carbon dioxide equivalence of 27,000 tonnes. The total amount of the same type of synthetic greenhouse gas

exported by the person has a carbon dioxide equivalence of 2,000 tonnes.

- The 2,000 tonnes of CO_2-e will be netted out from the person's liability.
- The person will be liable for 25,000 tonnes of CO_2-e (subject to any other relevant exclusion outlined below).

Example 1.12 Importer of synthetic greenhouse gas

The total amount of a particular synthetic greenhouse gas imported by a person has a carbon dioxide equivalence of 27,000 tonnes. The total amount of the same type of synthetic greenhouse gas exported by that person has a carbon dioxide equivalence of 30,000 tonnes.

- The 27,000 tonnes of CO_2-e will be netted out from the person's liability.
- The person will be liable for 0 tonnes of CO_2-e.

1.175 The references for Examples 1.11 and 1.12 are ***[Part 3, Division 3, clause 26]***, ***[Part 3, Division 3, clause 27].***

1.176 Where a person supplies an amount of synthetic greenhouse gas to another person, and the other person quoted their OTN in relation to the supply, the person's netted-out number equals the carbon dioxide equivalence of the amount supplied. ***[Part 3, Division 3, clause 26(9)]***, ***[Part 3, Division 3, clause 27(8)]*** This is consistent with the general principle that liability can be transferred to a person to whom an amount of synthetic greenhouse gas or eligible upstream fuel is supplied, where that person quotes the person's OTN in relation to the supply.

Liable entity – re-supplier of synthetic greenhouse gas

Application of provisions

1.177 As outlined above, a person who is supplied an amount of synthetic greenhouse gas by an importer or manufacturer of synthetic greenhouse gas may assume liability in respect of the gas by quoting their OTN in relation to the supply. ***[Part 3, Division 3, clause 28]***

1.178 Where the OTN holder then re-supplies an amount of the synthetic greenhouse gas to a third person who does not quote an OTN in relation to the supply, the OTN holder will incur a liability for that amount. ***[Part 3, Division 3, clause 28].*** In some circumstances the third person could be an OTN holder that does not quote an OTN.

1.179 The purpose of the provision is ensure that scheme obligations are not imposed on gases that are exported where exporters obtain synthetic greenhouse gas by way of supply from another entity in Australia.

1.180 Note: only entities that re-supply synthetic greenhouse gases or exporters of synthetic greenhouse gases will be permitted to quote an OTN in relation to the supply of synthetic greenhouse gases. Moreover, the synthetic greenhouse gas supplied under that OTN may only be re-supplied to another entity or exported.

Provisional emissions number

1.181 The provisional emissions number for a person that quotes an OTN for a supply of synthetic greenhouse gas is equal to the amount of the synthetic greenhouse gas that the person re-supplies (in CO_2-e) to entities that do not quote an OTN. The person is not liable for synthetic greenhouse gases that are exported or re-supplied to entities that quote an OTN.

Anti avoidance

1.182 Provisions which address schemes entered into with the substantial purpose of obtaining the advantage of the thresholds are described in Chapter 9 of the commentary. ***[Part 3, Division 2, clauses 23, 30]*** In brief, the benefit of the threshold provision may be lost.

Obligation Transfer Numbers

1.183 The issue, surrender and cancellation of OTNs are dealt with in Part 3, Division 5, Subdivision A. Subdivision B describes the method of quoting an OTN. Subdivisions C and D outline the circumstances in which an OTN must be quoted or is permitted to be quoted under the draft bill. General provisions that relate to the use and misuse of OTNs are in Subdivision E.

1.184 OTNs have a number of roles in transferring liability:

- OTNs allow certain people to assume liability for emissions from the combustion of particular fuels. ***[Part 3, Division 5, clauses 52, 56, 60-63]***

- OTNs permit entities to assume liability, if any arises, for certain fuels or synthetic greenhouse gases that are sequestered into a product (that is, used as feedstock) or used in a way that results in emissions that do not count towards

Australia's national inventory, such as export. ***[Part 3, Division 5, clauses 55, 57-58, 60-62, 64]***

- In the case of natural gas and liquid petroleum gas, OTNs move the bulk of scheme obligations from upstream suppliers (producers or importers) to re-suppliers who have access to accurate customer usage information. ***[Part 3, Division 5, clauses 53-54]***

- OTNs prevent double counting where entities transform one type of fuel into another type of fuel. ***[Part 3, Division 5, clause 59]***

Issue of an OTN

1.185 An OTN may be issued in one of two ways: as a result of an application, or on the Authority's own initiative. ***[Part 3, Division 5, clause 41]***

1.186 The draft bill specifies procedures and requirements relating to an application for an OTN. ***[Part 3, Division 5, clauses 42-43]***

1.187 The issue of an OTN on the Authority's own initiative will primarily occur where an entity is a large user of an eligible upstream fuel and hence will be required to quote an OTN. The Authority will have access to emissions data reported under the *National Greenhouse and Energy Reporting Act 2007* that will enable it to identify such entities. This will simplify the issue of OTNs to these entities by eliminating the application process.

1.188 When issuing an OTN, either as a result of an application or on the Authority's own initiative, the Authority must, before issuing an OTN:

- be satisfied that the applicant is, or is likely to be, required or permitted by the draft bill to quote an OTN in relation to the supply to the person of an amount of eligible upstream fuel or synthetic greenhouse gas

- have carried out 'the applicable identification procedure' in respect of the person. ***[Part 3, Division 5, clauses 44-45]***

1.189 An 'applicable identification procedure' is a procedure, set out in the regulations, that enables the Authority to verify the identity of an applicant.

1.190 An OTN issued to a person is not transferable. ***[Part 3, Division 5, clause 48]***

Cancellation or surrender of OTN

1.191 In certain circumstances a person may surrender an OTN with the written consent of the Authority. ***[Part 3, Division 5, clause 46]*** The Authority must only consent to the surrender of an OTN if satisfied that the person is not required or is unlikely to be required to quote an OTN.

1.192 This provision will enable a person that is permitted but not required to quote an OTN to surrender it if they no longer expect to quote it. It will also enable a person to surrender their OTN if they are no longer permitted or required to quote it.

1.193 The Authority may cancel an OTN that is held by a person that is not permitted or required to quote it, or is unlikely to be permitted or required to do so. ***[Part 3, Division 5, clause 47(2)]***

1.194 The Authority may also cancel an OTN if a person has breached a provision of the draft bill or an associated provision. It is anticipated that the Authority may take this step where there was an unacceptably high risk of further breaches to the draft bill or associated provisions relating to the use of that OTN.

1.195 The Authority must cancel a person's OTN if the person has ceased to exist, and immediately before the person ceased to exist the person held an OTN. ***[Part 3, Division 5, clause 47(3)]***

The OTN register

1.196 The Authority must keep an electronic register known as the OTN register. ***[Part 3, Division 5, clause 49]*** This register will be available for public inspection on the Authority's website. It will contain an entry for every current OTN. When an OTN is cancelled or surrendered the Authority must remove the entry from the register.

1.197 An entry in the OTN register will include an OTN, the identity of the person that was issued with that OTN, and the OTN holder's last known address. The OTN register will enable suppliers to confirm that an OTN is valid, and that it belongs to the person that quotes it.

Quoting an OTN

1.198 Quotation of an OTN in relation to a supply of eligible upstream fuel or synthetic greenhouse gas refers to the OTN holder making a statement to the supplier consisting of the words "quotation of OTN" followed by providing the OTN to the supplier. ***[Part 3, Division 5, clause 51(2)]***

1.199 The statement may be included in a contract, order or similar document and may be in electronic form. ***[Part 3, Division 5, clause 51(3)]***

1.200 After commencement of the Scheme (1 July 2010) an OTN quotation made in relation to a supply under contract must be made prior to entering into the contract. However, where a contract was entered into prior to Scheme commencement an OTN quotation may be made after the contract was entered into, but before Scheme commencement. This will enable entities that are required or permitted to quote an OTN and that entered into supply contracts prior to Scheme commencement to quote an OTN in relation to the supply. ***[Part 3, Division 5, clause 51(2)]***

1.201 Quotation of an OTN will be voluntary in some circumstances and mandatory in others.

1.202 A supplier must accept the quotation of an OTN where the quotation is mandatory for the OTN holder and may accept the quotation where it is voluntary.

Mandatory quotation of an OTN

1.203 Four types of entities will be required to quote an OTN*:*

- large users of eligible upstream fuels ***[Part 3, Division 5, clause 52]***
- re-suppliers of natural gas ***[Part 3, Division 5, clause 53]***
- re-suppliers of liquid petroleum gas ***[Part 3, Division 5, clause 54]***
- feedstock users of liquid petroleum gas (including refinery grade propene). ***[Part 3, Division 5, clause 55]***

1.204 Each provision that requires quotation of an OTN contains ancillary provisions relating to contravention of a requirement to quote an OTN. ***[Part 3, Division 5, clause 52(2)-(3)] [Part 3, Division 5, clause 53(2)-(3)] [Part 3, Division 5, clause 54(2)-(3)] [Part 3, Division 5, clause 55(2)-(3)]***

1.205 The purpose of these provisions is to provide an incentive for suppliers and recipients of eligible upstream fuel to comply with the requirement that an OTN be quoted in relation to a particular supply. Upon application by the Authority, the Federal Court may, if it decides that a person aids, procures, induces etc. a contravention of the requirement to quote an OTN in relation to a particular supply, order the person to pay the Commonwealth a civil penalty. ***[Part 21, clause 327]***

1.206 Where an entity is required to quote its OTN under the mandatory quotation provisions, the supplier must accept the quotation.

Note, however, that a supplier must not supply to a person who purports to quote their OTN, but the number is not the person's OTN as shown on the OTN Register. ***[Part 3, Division 5, clause 68]***

Large users of eligible upstream fuels (excluding users of liquid petroleum fuel)

1.207 For the purposes of determining whether an entity is required to quote an OTN for a supply of fuel, large users of eligible upstream fuels (large fuel users) are those entities that operate a facility that emitted 25 000 tonnes of CO_2-e or more from the combustion of a single type of eligible upstream fuel (other than liquid petroleum fuel) in the previous financial year. Entities that hold a liability transfer certificate in respect of such a facility are also large fuel users. Pro-rata thresholds apply for facilities that an entity operates for part of a year, or where an entity holds a liability transfer certificate in respect of a facility for part of a year. ***[Part 3, Division 5, clause 52]***

1.208 Entities will be able to ascertain whether they meet the threshold for large fuel users on the basis of their previous year's report made under the *National Greenhouse and Energy Reporting Act 2007*.

1.209 Large fuel users will be required to quote an OTN in relation to a supply of a fuel for a facility where that fuel contributed 25,000 tonnes of CO_2-e or more to the facility's greenhouse gas emissions in the previous year.

1.210 Large fuel users will not be required to quote an OTN for fuels that contributed less than 25,000 tonnes of CO_2-e to a facility's emissions in the previous year. This is to ensure that suppliers are not required to net out small amounts of fuel.

1.211 However in certain circumstances large fuel users will be permitted to quote their OTN in relation to fuels that contribute less than 25,000 tonnes of CO_2-e to a facility's emissions, as explained in the section below on voluntary quotation of an OTN.

Retailers of natural gas and marketers of liquid petroleum gas

1.212 Retailers of natural gas and marketers of liquid petroleum gas will be required to quote an OTN. ***[Part 3, Division 5, clauses 53-54]*** This will transfer the bulk of Scheme liabilities for these fuels to the entities that have customer usage information for these fuels and will ensure that these re-suppliers operate within equivalent market rules.

1.213 Arrangements for the transfer of Scheme obligations for natural gas that is traded through wholesale markets such as the Victorian gas

pool and the proposed short term trading market are not included in this draft bill. The Department of Climate Change is consulting with stakeholders on suitable arrangements and these will be addressed in the final legislation.

1.214 Marketers of liquid petroleum gas are those entities that re-supply liquid petroleum gas that is supplied to them from an import terminal bulk storage, petroleum refinery bulk storage or liquid petroleum gas separation plant bulk storage. ***[Part 3, Division 5, clause 54]*** Some entities that the liquid petroleum gas industry commonly considers to be marketers (those that run vertically integrated operations with bulk storage facilities) will not meet this definition as "supply" does not include intra-company transfers. Nevertheless, these entities will have Scheme obligations for the liquid petroleum gas they supply by way of their status as upstream fuel suppliers. ***[Part 3, Division 4, clause 33]***

Feedstock users of liquid petroleum gas

1.215 Feedstock users of liquid petroleum gas, including feedstock users of refinery grade propene, will also be required to quote an OTN to their suppliers of these fuels. ***[Part 3, Division 5, clause 55]***

1.216 Feedstock users often consume significant quantities of these fuels, and there are a limited number of suppliers to these industries. These circumstances present risks that significant Scheme liabilities could be imposed for large quantities of fuel that will not result in emissions. As such, feedstock users of liquid petroleum gas (including refinery grade propene) will be required to quote an OTN.

1.217 The draft bill gives effect to this provision for liquid petroleum gas used as feedstock, but not for refinery grade propene. This will be addressed in the final legislation.

Voluntary quotation of an OTN

1.218 Seven types of entities will be permitted, but not required, to quote an OTN in relation to a particular supply of eligible upstream fuel or synthetic greenhouse gas. ***[Part 3, Division 5, Subdivision D]*** These are:

- large users of eligible upstream fuels ***[Part 3, Division 5, clause 56]***
- packagers of fuels for use as solvents or other products that are not intended for combustion ***[Part 3, Division 5, clause 57]***
- entities that use eligible upstream fuels as feedstock to manufacture other products, or in ways that do not result in

emissions of greenhouse gases to the atmosphere ***[Part 3, Division 5, clause 58]***

- entities that transform eligible upstream fuels from one type into another ***[Part 3, Division 5, clause 59]***
- exporters and intermediate suppliers of certain fuels ***[Part 3, Division 5, clauses 60-62]***
- intermediate suppliers of synthetic greenhouse gases ***[Part 3, Division 5, clause 63]***
- exporters of synthetic greenhouse gases. ***[Part 3, Division 5, clause 64]***

Large users of eligible upstream fuels

1.219 A large user of eligible upstream fuel (large fuel user) may be permitted to make a voluntary quotation of an OTN for a supply of fuel. This will occur if, at the time of the supply, the entity operates a facility that in the previous financial year had greenhouse gas emissions from combustion of one type of eligible upstream fuel of at least the amount, in CO_2-e, specified in the regulations. ***[Part 3, Division 5, clause 56]***

1.220 The threshold that defines a large fuel user for the purposes of voluntary quotation of an OTN will be prescribed in regulations. The Government's intent is to set this threshold initially at 25,000 tonnes of CO_2-e or less.

1.221 Setting the threshold at this level will enable large fuel users that are required to quote an OTN for one type of fuel supplied to a facility to quote an OTN for other fuels used at the facility. They will also be able to quote an OTN when purchasing fuel for other facilities that do not exceed the single fuel threshold. ***[Part 3, Division 5, clause 56]*** This will allow simpler billing arrangements where a large fuel user obtains more than one type of fuel from a supplier, or purchases fuel from one supplier for use at more than one facility.

1.222 Some entities may expect their emissions to exceed the threshold in a particular year, even though they do not satisfy the threshold test for the previous year. This may occur, for example, where an entity expects to increase production at an existing facility or establish a new facility. These entities will be able to apply to the Authority to gain status as a large user of eligible upstream fuel – an "approved person". The Authority will only approve an application if satisfied that emissions are likely to exceed the threshold in the year to which the application relates. ***[Part 3, Division 5, clause 56]***

1.223 The threshold may be lowered over time to allow a greater range of entities to manage their scheme obligations voluntarily.

Example 1.13 Large user of eligible upstream fuel with prior reporting history

Company X has operational control over a coal mine. In 2011 emissions from the coal mine comprise:

- 40 000 tonnes of CO_2-e of fugitive emissions
- 30 000 tonnes of CO_2-e from use of diesel
- 2 000 tonnes of CO_2-e from use of petrol.

Company X also has operational control over another mine which is a facility in its own right. In 2011 emissions from this second mine comprise:

- 20 000 tonnes of CO_2-e of fugitive emissions
- 15 000 tonnes of CO_2-e from use of diesel
- 1 000 tonnes of CO_2-e from use of petrol.

In 2012 Company X is permitted to quote an OTN for its diesel use at the first mine because, in 2011, its emissions from diesel use at that mine exceeded the single fuel threshold specified in the regulations. Because emissions from one fuel exceeded the threshold, Company X is also permitted to quote an OTN for its petrol use at that mine. Company X is also permitted to quote an OTN for its diesel and petrol use at the second mine, even though emissions attributable to any one type of fuel used at the second mine do not exceed the single fuel threshold specified in the regulations.

The company establishes a fuel supply contract with a fuel company for the diesel and petrol used at both mines. The company makes a voluntary OTN quotation in that contract which is accepted by the supplier. The company must then manage scheme obligations for all fuel supplied under this contract.

Example 1.14 Start-up company that expects to be a large user of eligible upstream fuel

A company is in the process of commissioning a gas fired electricity plant. It expects to emit 500 000 tonnes of CO_2-e of greenhouse gas emissions in its first year of operation. The company applies to the Authority for an OTN and submits all information and documents specified in the regulations. The Authority assesses the application and

> decides that it is likely that the company's emissions from natural gas combustion will exceed the threshold value specified in the regulations. The Authority, by written notice, declares that the company is an *approved person*. The company is permitted to quote an OTN for the natural gas it purchases for its new electricity plant.

Packagers of fuels for use as solvents or other products that are not intended for combustion

1.224 The quotation of an OTN will be voluntary for entities that package fuel for use as solvents or other products that are not intended for combustion. ***[Part 3, Division 5, clause 57]*** These entities will largely comprise solvent packagers that are currently eligible for a fuel tax credit under section 41.10(2) of the *Fuel Tax Act 2006.*

1.225 In order to be permitted to quote an OTN under this provision, a person must carry on a business that involves packaging fuel for a non-combustion related use and must meet the conditions specified in the regulations. ***[Part 3, Division 5, clause 57]***

1.226 It is intended that the regulations will specify conditions similar to those in regulations made under section 40.10(2) of the *Fuel Tax Act 2006.* The regulations will be designed to ensure that only those entities that package fuels for use in applications that do not result in emissions of greenhouse gases to the atmosphere will be permitted to quote an OTN.

1.227 Where an entity re-supplies fuel that has been packaged in accordance with the regulations, no liability will apply to the supply. ***[Part 3, Division 4, clause 37(4)]***

Use of fuel in manufacturing other products etc

1.228 A person may quote an OTN if they use fuels to manufacture products in which all or part of that fuel is sequestered, such as where a fuel is used as a feedstock to make plastic. Entities that use fuels in other ways that do not result in emissions of greenhouse gases to the atmosphere may also quote an OTN. An example of this type of use is the use of diesel as a flocculent in minerals processing. ***[Part 3, Division 5, clause 58]***

1.229 The circumstances under which these entities will be permitted to quote an OTN do not require that the fuel is to be used for a specific purpose. This recognises that entities permitted to quote an OTN under this provision commonly combust a portion of the fuel supplied to them.

1.230 While these entities will be permitted to quote an OTN for all supplies of the particular fuel, they will incur scheme obligations for any

greenhouse gas emissions from the use of that fuel. Liability for these emissions will be imposed under the direct emitter provisions, or under the application to own use provisions where the direct emitter provisions do not apply. ***[Part 3, Division 2] [Part 3, Division 4]***

Transformation of fuel

1.231 An entity that transforms one type of eligible upstream fuel into another type of eligible upstream fuel, for example manufacturing coke oven coke from black coal, will be liable for the supply of the transformed fuel to entities that do not quote an OTN. ***[Part 3, Division 4, clause 35]*** However, where a fuel transformer obtains pre-transformed fuel from another entity, liability will be imposed on that supply unless the fuel transformer is permitted to quote an OTN. ***[Part 3, Division 4, clause 33]***

1.232 For this reason, entities that undertake recognised fuel transformations will be permitted to quote an OTN. ***[Part 3, Division 5, clause 59]*** Recognised fuel transformation processes are defined in the draft bill. ***[Part 1, clause 5, definition of 'recognised transformation']*** Additional fuel transformations that involve transforming one type of eligible upstream fuel into another type of eligible upstream fuel can be added through the regulations.

Export or re-supply of eligible upstream fuels

1.233 Intermediaries are present in certain fuel supply chains, including the supply chain for black coal. Entities that are permitted or required to quote an OTN and that are supplied fuel by an intermediary, would not be able to assume scheme obligations for fuels unless their supplier is also permitted to quote an OTN. Furthermore, intermediaries that export fuels would incur the cost of scheme obligations if they were unable to quote an OTN. For these reasons, certain intermediaries will be permitted to quote an OTN. ***[Part 3, Division 5, clauses 60-62]***

1.234 Intermediaries in the coal supply chain and liquefied natural gas supply chain will be permitted to quote an OTN. ***[Part 3, Division 5, clauses 60-61]*** The regulations will allow for inclusion of intermediaries for additional fuel types where this is needed to allow downstream entities to assume liability for fuel supplied to them, or where an intermediary exports fuel. ***[Part 3, Division 5, clause 62]***

Exporter or re-supplier of synthetic greenhouse gases

1.235 A person will be permitted to quote an OTN for a supply of synthetic greenhouse gases in two circumstances. The first is where a person carries on a business re-supplying synthetic greenhouse gases and

the quotation is for an amount of synthetic greenhouse gas that will be re-supplied to a third person. ***[Part 3, Division 5, clause 63]*** The second circumstance is where a person carries on a business exporting synthetic greenhouse gases and the quotation is for an amount of synthetic greenhouse gas that will be exported by that person. ***[Part 3, Division 5, clause 64]*** The intention of allowing the quotation of an OTN under these circumstances is to ensure that synthetic greenhouse gases that are exported are not covered by the Scheme.

1.236 In practice, an entity that both exports synthetic greenhouse gases and supplies synthetic greenhouse gases within Australia will be able to quote an OTN when purchasing synthetic greenhouse gases from their supplier. However, the entity will only be liable for the portion of synthetic greenhouse gas re-supplied domestically.

Example 1.15 Exporter of synthetic greenhouse gases

A company manufactures air conditioners that contain synthetic greenhouse gases. The company exports a portion of its product and supplies the other portion on the domestic market. When purchasing synthetic greenhouse gas refrigerants from their supplier (an importer of synthetic greenhouse gases) the company quotes their OTN. The importer will not be liable for the synthetic greenhouse gas supplied to the company. The company will be liable for the synthetic greenhouse gases (in CO_2-e) within the air conditioning equipment it supplies to the domestic market.

Quotation of bogus OTN

1.237 If a person purports to quote a number as their OTN for a supply, and that number is not shown in the OTN register as the person's OTN, the supplier must not supply eligible upstream fuel or synthetic greenhouse gas to the person. ***[Part 3, Division 5, clause 68(2)]***

1.238 Suppliers will therefore need to check the details in the OTN register at the time an OTN is quoted, and ensure that the entity quoting it matches the identity details in the register against that OTN.

1.239 Upon application by the Authority, the Federal Court may order a person to pay the Commonwealth a civil penalty if it decides that the person has, for example, aided a contravention of the requirement that a person must not quote a bogus OTN or supply eligible upstream fuel and synthetic greenhouse gas to a person that quotes a bogus OTN. ***[Part 3, Division 5, clause 67(2)-(3)] [Part 21, clause 327]***

1.240 For evidentiary purposes the Authority may supply a copy of or extract from the OTN register certified by an official of the Authority to be a true copy or true extract. This certified copy or extract will be

admissible as evidence in all courts and proceeding without further proof or production of the original. ***[Part 3, Division 5, clause 50]***

Rejection of OTN

1.241 In certain circumstances a supplier is required or permitted to reject an OTN. These circumstances are outlined below.

Rejection of OTN - re-supply of eligible upstream fuel

1.242 If a person supplies eligible upstream fuel to a second person who does not quote an OTN for the supply, and the second person then re-supplies all or part of that fuel to a third person who quotes an OTN, the second person must reject the OTN quotation. ***[Part 3, Division 5, clause 65]***

1.243 The purpose of this clause is to avoid double counting. In the absence of this provision, the third person or another person further down the supply chain could incur liability for an amount of fuel or synthetic greenhouse gas for which a liability has already been incurred.

1.244 The effect of a supplier rejecting the quotation of a person's OTN under this clause is that, if the supply occurs, the supply is taken to have occurred as if the person did not quote their OTN for the supply. ***[Part 3, Division 5, clause 65(3)]***

1.245 This clause contains ancillary provisions relating to contravention of the clause. ***[Part 3, Division 5, clause 65(4)-(5)]***

1.246 The purpose of these ancillary provisions is to provide an incentive for suppliers and recipients of eligible upstream fuel to comply with the requirement that an OTN be rejected in the circumstance described. Upon application by the Authority, the Federal Court may, if it decides that a person has, for example, aided a contravention of the requirement to reject an OTN in relation to a particular supply, order the person to pay the Commonwealth a civil penalty. ***[Part 21, clause 327]***

Rejection of voluntary quotation of OTN

1.247 A supplier may, in accordance with the regulations, reject the quotation of a person's OTN for a supply of eligible upstream fuel if that quotation is not required. ***[Part 3, Division 5, clause 66]*** The regulations will specify a method for rejection.

1.248 The effect of a supplier rejecting the quotation of an OTN under this clause is that, if the supply occurs, it is taken to have occurred as if the person did not quote their OTN for the supply.

1.249 A supplier does not need any particular reason to reject the quotation of a voluntary OTN. However, circumstances under which a supplier may wish to reject a voluntary OTN quotation include:

- the supplier does not have administrative arrangements that would allow the netting out of amounts of fuel supplied to OTN holders
- for reasons of administrative simplicity, the supplier wishes to manage scheme obligations for all fuel that it supplies.

Misuse of OTN

1.250 The mere issue of an OTN does not permit a person to quote it. When a person quotes an OTN for a particular supply of eligible upstream fuel or synthetic greenhouse gas the person must, at the time of quotation, be permitted or required to do so. An OTN holder breaches the provisions in the draft bill if they quote an OTN in circumstances where they are not required or permitted to do so. ***[Part 3, Division 5, clause 67]***

1.251 If a person quotes an OTN in circumstances where they are not required or permitted to do so, the validity of the transaction is not affected by the breach. That is, the person will retain a liability for that transaction. ***[Part 3, Division 3, clause 29]***, ***[Part 3, Division 4, clause 40]***, ***[Part 3, Division 5, clause 67(4)]***.

1.252 Upon application by the Authority, the Federal Court may order a person to pay the Commonwealth a civil penalty, if it decides that the person has, for example, aided a contravention of the requirement not to quote an OTN in circumstances where they are not required or permitted to do so. ***[Part 3, Division 5, clause 67(2)-(3)] [Part 21, clause 327]***

1.253 This provides an incentive for suppliers and recipients of eligible upstream fuel and synthetic greenhouse gas to comply with the requirement that an OTN must only be quoted in circumstances where a person is required or permitted to do so under the draft bill.

Reporting requirements

1.254 The *National Greenhouse and Energy Reporting Act 2007* will be amended to allow regulations to specify reporting requirements for entities that either use or accept the quotation of an OTN. Examples of the type of information that may be required by regulations are quantities of different types of fuel supplied to a person under an OTN and re-supplied to another person including separate amounts supplied to different OTNs. (See the consequential amendments bill, Schedule 1, Part 2, item 181)

Liability transfer certificates

1.255 In order to apply for a liability transfer certificate an entity must pass either the Category A or Category B transfer test as outlined below. This section also outlines general criteria and processes in relation to liability transfer certificates. ***[Part 3, Division 6]***

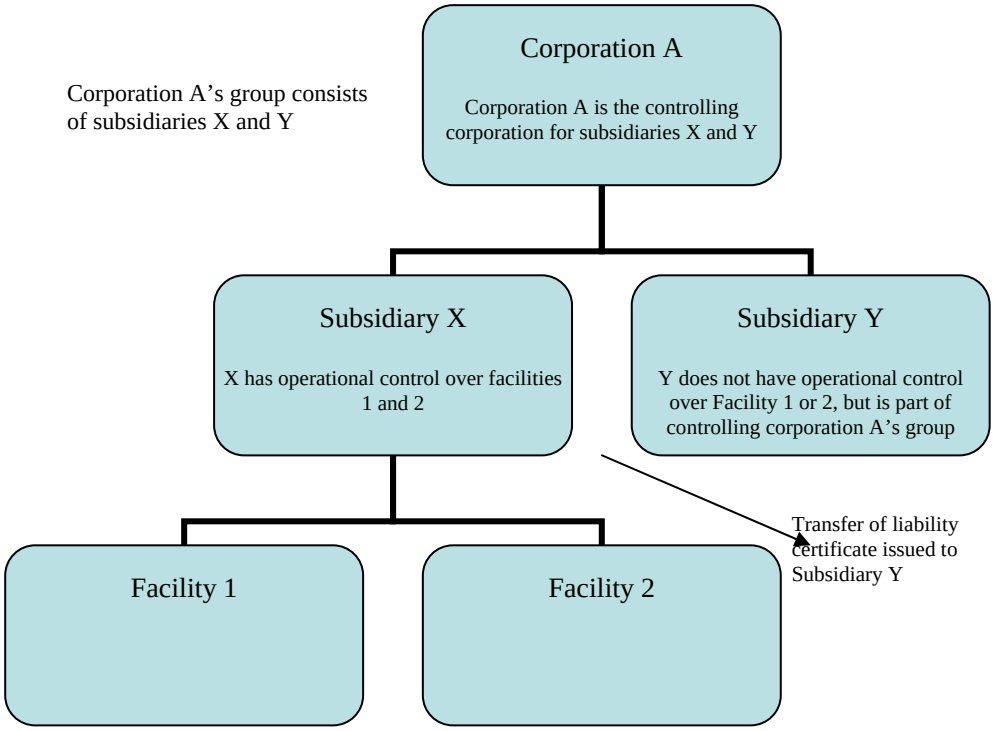
Transfer of liability to another member of a controlling corporation's group

1.256 Division 6, Subdivision A applies to corporations only. This Subdivision is intended to enable the transfer of Scheme liability from a controlling corporation to a member of its corporate group, particularly in the instance where placing Scheme obligations on the controlling corporation would significantly impair the ability of the controlling corporation, or a member of its group, to pass through carbon costs in existing contracts and convey efficient price signals to end users. This is the category A transfer test ***[Part 3, Division 6, clause 69].***

1.257 Under Subdivision A, a controlling corporation must consent to the making of an application for a liability transfer certificate by a company in its corporate group. ***[Part 3, Division 6, clause 70(3)]*** Where a liability transfer certificate is issued the controlling corporation is taken to have given a statutory guarantee for the payment of any administrative penalty for a unit shortfall for the relevant financial year and any late payment penalty for that company ***[Part 6, Division 4, clause 138]*** This provision ensures that there is always a liable entity under the Scheme for a covered facility and prevents controlling corporations from avoiding liability under the Scheme by transferring liability to a member of their corporate group.

Example 1.16

Diagram 1.1



Transfer of liability certificate is issued for Subsidiary Y in relation to Facility 2.

Subsidiary Y takes on all obligations and liability for Facility 2 under the Scheme and under the *National Greenhouse and Energy Reporting Act 2007* – this includes reporting in relation to emissions, energy production and energy consumption.

Corporation A will not have obligations or liability for Facility 2 under the Scheme and under the *National Greenhouse and Energy Reporting Act 2007*.

Corporation A will, however, have consented to the application for the transfer and in doing gives a statutory guarantee against liability incurred by Subsidiary Y.

Facility 2 will continue to form part of Corporation A's group for the purposes of meeting the audit threshold under the Scheme for entities with a liability of 125,000 tonnes or more of greenhouse gas in CO2-e and for meeting the *National Greenhouse and Energy Reporting Act 2007* group thresholds.

Transfer of liability to a company that has financial control over a facility

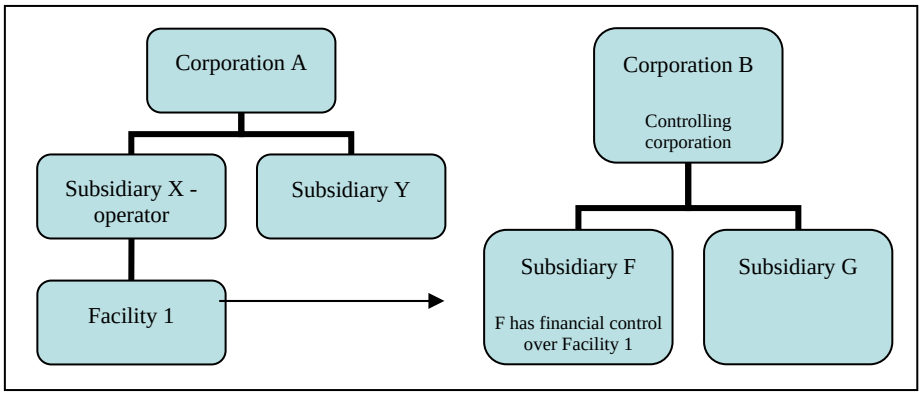
1.258 Division 6, Subdivision B as drafted applies to corporations and statutory authorities of the Commonwealth, States and Territories. It outlines the circumstances in which liability can be transferred from a controlling corporation, to a corporation incorporated in Australia or to a statutory authority that has financial control over a facility. It is intended that this Division will be expanded to allow a transfer from any person with operational control to any person with financial control.

1.259 In the majority of circumstances, the entity with operational control over a facility will also be the entity with financial control of that facility. However, in some circumstances, for example contract mining and pipeline operations, the entity with financial control of a facility contracts out the operation of a facility to another entity. The operator will then generally have operational control over the facility and therefore liability for the facility under the Scheme. As the entity with financial control of a facility may have the greatest influence over emissions arising from the covered facility, it is appropriate to allow that entity to take on liability for the facility with the agreement of the operator of the facility.

1.260 In line with the underlying purpose of the Scheme, to reduce emissions, an entity taking on liability must have a significant connection to a facility that encompasses the ability to reduce emissions from that facility. This is why the transfer of liability provisions have been limited to members of a controlling corporation's group and entities with financial control of a facility. Financial control is intended to encompass an entity that has significant ability to control a facility through financial means only. It is not intended to include an agent or person acting on behalf of an entity that has financial or operational control of a facility. ***[Part 3, Division 6, clause 81]***

1.261 The meaning of financial control recognises that more than one entity may have financial control over a facility. For example several persons may be participants in a joint venture that collectively have financial control of a facility. In these circumstances, the entity with equal or greatest financial control is intended to be the entity that will be able to apply for a liability transfer certificate.

Diagram 1.2



Subsidiary F, which is part of Controlling Corporation A's group, has financial control over Facility 1. Subsidiary F (with consent from Corporation A and Corporation B) applies for a liability transfer certificate.

A certificate is issued and Subsidiary F takes on takes on all obligations and liability for Facility 1 under the Scheme and under the *National Greenhouse and Energy Reporting Act 2007* – this includes reporting in relation to emissions, energy production and energy consumption.

Corporation A will not have obligations or liability for Facility 1 under the Scheme and under the *National Greenhouse and Energy Reporting Act 2007*.

Facility 1 will form part of Corporation B's group for the purposes of meeting the audit threshold under the Scheme for entities with a liability of 125,000 tonnes or more of greenhouse gas in CO2-e and for meeting the *National Greenhouse and Energy Reporting Act 2007* group and facility thresholds.

Liability transfer certificates – general

1.262 In order to apply for a liability transfer certificate an entity must pass either the Category A or Category B transfer test as outlined above. Note that a liability transfer certificate may only be issued for a single facility. If an entity wanted to transfer liability for more than one facility they would have to apply for a liability transfer certificate for each facility for which that it wants to transfer liability. ***[Part 3, Division 6, clause 69] [Part 3, Division 6, clause 73].***

1.263 An entity must also meet the criteria for the issue of a liability transfer certificate as the Authority cannot issue a certificate unless it is satisfied that an entity has met these criteria. ***[Part 3, Division 6, clause 72] [Part 3, Division 6, clause 76]*** Criteria have been included to maintain Scheme integrity by ensuring that an entity has the capacity, access to information, and financial resources to comply with its obligations under the Scheme legislation as well as the *National Greenhouse and Energy Reporting Act 2007*.

1.264 Including a criterion that an entity must have the financial resources to comply with obligations imposed on it ensures that a controlling corporation does transfer liability to a company that cannot meet Scheme obligations in order to avoid or delay liability. This test is not, however intended to involve an exhaustive explanation by the applicant of its financial situation. ***[Part 3, Division 6, clause 72] [Part 3, Division 6, clause 76]***

1.265 Obligations for reporting under the *National Greenhouse and Energy Reporting Act 2007* in relation to the facility for which a liability transfer certificate has been issued will be transferred to the holder of a liability transfer certificate. This includes any reporting obligations that would ordinarily apply to the entity with operational control, and depending on thresholds met under the *National Greenhouse and Energy Reporting Act 2007* may include reporting obligations in relation to greenhouse gas emissions, energy production and energy consumption. The draft consequential amendments bill will give effect to these provisions. (See the consequential amendments bill, Schedule 1, Part 2, items 175-181) The provisions relating to reporting obligations in the draft bill do not reflect this policy. This will be addressed in the final legislation. The criteria in relation to capacity and access to information for compliance with the *National Greenhouse and Energy Reporting Act 2007* are included because of these reporting requirements.

1.266 An application to obtain a liability transfer certificate must be made in writing in a form approved by the Authority. An application by a corporate entity must be accompanied by the written consent of its controlling corporation. The application must also include any information and documents that are specified in regulations. This is intended to cover information and documents that support an entity's application and demonstrate that the entity meets the criteria for the issue of a liability transfer certificate. ***[Part 3, Division 6, clause 70] [Part 3, Division 6, clause 74]***

1.267 The Authority may request further information in relation to an application within a period specified in a notice given by the Authority. This is to assist the Authority in its decision making capacity; as indicated above the Authority must not issue a liability transfer certificate unless it

is satisfied that an entity has met the criteria for the issue of that certificate. If the applicant does not meet this request within the time specified, the Authority may refuse to consider the application or refuse to take any action, or any further action, in relation to the application. ***[Part 3, Division 6, clause 71] [Part 3, Division 6, clause 75]***

1.268 The Authority is required to take all reasonable steps to ensure that a decision is made on an application for a liability transfer certificate within 90 days of receiving an application or within 90 days of being given further information. The Authority must inform an applicant in writing of a decision to refuse to issue a transfer of liability certificate. ***[Part 3, Division 6, clause 72] [Part 3, Division 6, clause 76]***

1.269 An application for a liability transfer certificate will be able to be made as soon as the provisions in the draft bill commence, which is 28 days after Royal Assent. A liability transfer certificate may come into force on the start day specified in the certificate. The start day may be earlier than the day on which the certificate was issued provided that it is within the same financial year. This ensures that liability cannot be transferred from a financial year that has already passed and allows entities to obtain a liability transfer certificate for an entire financial year regardless of when the application is made or the certificated is issued during that financial year. ***[Part 3, Division 6, clause 77]***

1.270 The start date may only be earlier than the day on which the certificate is issued if the applicant and the parties referred to consent to the specification of that start day. ***[Part 3, Division 6, clause 77]*** This ensures that all entities that may be liable under the Scheme and the Authority know and agree who is liable and when.

1.271 Once made, a liability transfer certificate remains in force indefinitely subject to provisions relating to surrender of a liability transfer certificate and cancellation of a liability transfer certificate. ***[Part 3, Division 6, clause 77]***

1.272 If an entity wishes to surrender a liability transfer certificate it must obtain written consent from the Authority to do so. The Authority must not consent to the surrender unless:

- the controlling corporation that agreed to the making of the certificate agrees to the surrender, and
- the certificate has been in force for at least four years, or
- certificate has been in force for less than four years, but the Authority is satisfied that there are special circumstances that warrant the giving of its consent to the surrender

[***Part 3, Division 6, clause 78]***

1.273 The Authority must, by written notice, cancel a liability transfer certificate in the following circumstances:

- if a company ceases to pass a Category A or B transfer test, or
- if a company has not paid an administrative penalty for a unit shortfall under clause 133 of the draft bill, or
- if the company has become an externally-administered body corporate (within the meaning of the *Corporations Act 2001*), or
- if regulations specify one or more other grounds for cancellation and at least one of those grounds is applicable to the company

[Part 3, Division 6, clause 79]

1.274 The cancellation of a liability transfer certificate will result in future obligations and liability returning to the entity that would have had obligations and liability in the absence of the liability transfer certificate. [***Part 3, Division 6, clause 78]***

1.275 A liability transfer certificate cannot be surrendered unless the certificate has been in force for at least 4 years, or if the Authority is satisfied that there are special circumstances that warrant the giving of consent to the surrender of the certificate. The transfer of a liability transfer certificate for a minimum of 4 years supports the Scheme's integrity by ensuring a consistent liable entity and prevents multiple transfers of liability that may be aimed at avoiding liability.

1.276 Holding a liability transfer certificate for a minimum of 4 years aligns with the policy position that once an entity chooses to use Method 2 for a particular source in respect of a particular facility, that methodology will be the minimum standard for that particular source at that particular facility for that entity, for a period of four years.

1.277 As stated above an entity taking on liability must have a significant connection to a facility that encompasses the ability to reduce emissions from that facility. For this reason a liability transfer certificate can only be issued by the Authority and is not transferable ***[Part 3, Division 6, clause 80]***.

Australian boundaries

1.278 The Scheme will extend to every external Territory. ***[Part 1, clause 10]***

1.279 It will extend to a matter relating to the exercise of Australia's sovereign rights in the exclusive economic zone or the continental shelf. ***[Part 1, clause 11]***

1.280 This means that those responsible for carbon capture and storage facilities in the exclusive economic zone or the continental shelf will be responsible under the general provisions of the draft bill for any emissions from these facilities.

1.281 However, the Scheme will not apply to the extent that its application would be inconsistent with the exercise of rights of foreign ships in the territorial sea, exclusive economic zone or waters of the continental shelf in accordance with the United Nations Convention on the Law of the Sea. ***[Part 1, clause 12]***

1.282 The Government is considering whether the Scheme should include specific provisions relating to activities in the Joint Petroleum Development Area and the Greater Sunrise Oil and Gas Field (and pipelines associated with them) in the light of Australia's international obligations. The final decision on this issue will be included in the final bill prepared for introduction.

Chapter 2
Scheme caps, gateways and emissions units

Outline of chapter

2.1 This chapter discusses the national scheme caps and national scheme gateways, and nature of the various emissions units (domestic and international) recognised in the draft bill. It explains how these units can be issued and transferred. It also explains which can be surrendered.

2.2 It relates particularly to Part 2 and some clauses in Part 4 of the draft bill.

Context

2.3 The Carbon Pollution Reduction Scheme is a cap and trade scheme. It involves setting a national trajectory (which is referred to in the objects clause ***[Part 1, clause 3]***), and setting national scheme caps and gateways. The objects clause is discussed in the General Outline of this commentary. A limited number of emissions units are issued and liable entities are required to surrender an equal number of these units to account for their emissions. The emissions units are tradable, establishing a carbon market that allows emissions units to be allocated to the most highly valued uses across the economy. Therefore, determining the emissions units that can be used for surrender is fundamental to the operation of the scheme.

2.4 The Kyoto Protocol is an international agreement governing climate change, providing among other things a framework for an international cap and trade scheme. Australia has an obligation to retire emissions units referred to as Kyoto units to meet its Kyoto target. The Kyoto Protocol also establishes three 'flexibility mechanisms'. These 'flexibility mechanisms' result in the issue of Kyoto units which can be traded between Kyoto Parties and used towards meeting their emissions reduction targets. Kyoto Parties can also allow for legal entities to participate in the trade of Kyoto units.

2.5 Allowing for Kyoto units to be used for surrender in the Australian Carbon Pollution Reduction Scheme creates a link between this

Scheme and the international market for Kyoto units. This allows liable entities to access lower cost abatement opportunities wherever they occur in the world and allows for emission reduction targets to be achieved in a flexible and cost-effective way, without reducing its environmental integrity.

2.6 The Kyoto Protocol includes a requirement that Australia's use of the flexibility mechanisms be supplemental to its domestic actions. This means that Australia must take some meaningful domestic action to meet its emissions reduction target, and cannot rely solely on the flexibility mechanisms. Projections of Australia's greenhouse gas emissions for the first commitment period indicate Australia's reliance on the flexibility mechanisms to meet the target is expected to be minimal. Australia has undertaken a range of measures to reduce domestic greenhouse gas emissions, in addition to the Carbon Pollution Reduction Scheme, and will continue to do so. Collectively, these measures represent significant domestic action.

Summary

2.7 The national scheme caps and gateways will be set in regulations. The matters relevant to specifying the scheme caps and gateways are listed and discussed in this Chapter.

2.8 Australian emission units will be created for the purpose of the scheme. These will have a number of characteristics which ensure transparent and secure property rights.

2.9 Australian emissions units will be issued by the Authority on behalf of the Commonwealth in the Registry. Australian emissions units can then be transferred between Registry accounts and surrendered.

2.10 The draft bill recognises the emissions units created under the Kyoto Protocol and sets out how these units can be issued and transferred. Some types of Kyoto units can be surrendered for compliance purposes while others cannot. Nonetheless all Kyoto units can be held and transferred within the Registry.

Detailed explanation of new law

National targets and Scheme caps

2.11 Part 2 of the draft bill sets out arrangements for national scheme caps and national scheme gateways. It commences with a simplified outline ***[Part 2, clause 13].*** The purpose of national scheme gateways is to provide guidance for longer term cap-setting, while still retaining some flexibility over where future scheme caps can be set. National scheme caps and national scheme gateways will exist within a broader policy framework in relation to national emissions targets, and Australia's international obligations and objectives.

2.12 The Scheme involves setting a national scheme cap for a particular year and issuing units equal to that cap. The scheme cap for a particular year is a quantity of greenhouse gases that has a carbon dioxide equivalence of a specified number of tonnes.

2.13 Scheme caps will be lower than the emissions path required to meet any national emissions targets because some emissions sources are not covered by the Scheme (primarily emissions from agriculture and deforestation, or some below-threshold emissions from waste, industrial processes or fugitive emissions). Therefore, the same factors that the Government takes into account in setting the national emissions trajectory need to be taken into account when setting caps, because of the wide coverage of the Scheme.

2.14 Detailed scheme cap numbers for each financial year will be specified in regulations ***[Part 2, clause 14]***. The Government intends that these be consistent with the 2020 and 2050 national emissions targets. The Minister will be required to take all reasonable steps to ensure that regulations to specify the scheme cap numbers for the first five years of the scheme are made before 1 July 2010 ***[Part 2, clause 14(2)]***. The purpose of this requirement is to provide market certainty. In a similar vein, for all subsequent financial years, the Minister is required to take all reasonable steps to ensure that regulations declaring the scheme cap number are in place at least five years before the end of the relevant year ***[Part 2, clause 14(3)]***.

2.15 In the event that there is no scheme cap number for a year beginning on or after 1 July 2015, then the scheme cap number will be 99% of the scheme cap number for the previous year, except:

- where this number is greater than the upper bound of the gateway for the current year the scheme cap is equal to the upper bound of the gateway *or*

- where this number is less than the lower bound of the gateway, the scheme cap is equal to the lower bound of the gateway ***[Part 2, clause 14(4)]***.

2.16 In the above arrangement, the scheme caps that apply by default when scheme caps are not prescribed in regulations will always fall within the scheme gateways.

2.17 In making a recommendation to the Governor-General about scheme cap regulations, the Minister must have regard to Australia's international obligations under the United Nations Framework Convention on Climate Change and the Kyoto Protocol ***[Part 2, clause 14(5)(a)]***. The scheme will be the primary means through which Australia will aim to meet its international obligations, and so this is a mandatory criterion to take into account.

2.18 The Minister must also have regard to the most recent report of the independent reviews conducted under Part 25 of this draft bill. These reviews, by the expert advisory committee, will advise on whether national targets relating to emissions of greenhouse gases should be changed or extended ***[Part 25, clause 353(1)(b)]*** and on regulations setting caps and gateways ***[Part 25, clause 353(1)(c) and (d)]***.

2.19 While taking into account Australia's international obligations and the review report is a minimum requirement, the Minister has discretion to also have regard to a number of other factors. It is the Government's policy to set targets for national greenhouse gas emissions, as well as caps, which are calibrated in light of the extent of international action on climate change. However, within these bounds, there is room for discretion to take into account additional domestic factors, including economic implications and the extent of voluntary action. Specifically, the Minister may have regard to:

- The principle that fair and effective global action to stabilise atmospheric concentrations of greenhouse gases at around 450 parts per million of carbon dioxide equivalence or lower is in Australia's national interest ***[Part 2, clause 14(5)(c)(i)]***. The White Paper identified environmental integrity as a key factor in making decisions about the emissions trajectory. This longer term, global goal is important for cap-setting as Australia seeks to influence, and eventually play its full part in, international agreements that will deliver such an

outcome. The Government has chosen its medium term target range taking into account the following factors:

– that achieving a global commitment to emissions reductions of this order appears unlikely in the next commitment period; and

– that the most prospective pathway to this goal is to embark on global action that reduces the risks of dangerous climate change and builds confidence that deep cuts in emissions are compatible with continuing economic growth and improved living standards.

- Progress towards, and development of, comprehensive global action under which all major economies commit to substantially restrain emissions and advanced economies take on reductions comparable to Australia ***[Part 2, clause 14(5)(c)(ii)]***.

  – The White Paper stated that targets and trajectories should support Australia's international negotiating objectives and be consistent with international obligations. In the White Paper, the Government made a policy commitment to reducing Australia's national emissions by between 5 and 15% below 2000 levels by 2002. The top of the range represents a minimum (unconditional) commitment to reduce emissions to 5% below 2000 levels by 2020 (projected to be a 27% reduction in per capita terms). The bottom of the range represents a commitment to reduce emissions by up to 15% below 2000 levels by 2020 (projected to be a 34% reduction in per capita terms) in the context of global agreement under which all major economies commit to substantially restrain emissions and advanced economies take on reductions comparable to Australia.

  – As caps are extended over time, decisions must be made as to where within this range caps should lie, taking into account progress in international negotiations. In the longer term, the Government recognises that ambitious global action is in Australia's national interest. In the event that a comprehensive global agreement were to emerge over time, involving emissions commitments and actions by both developed and developing countries that are consistent with long-term stabilisation of atmospheric concentrations of greenhouse gases at 450 ppm CO2-e or lower, Australia is prepared to establish its post-2020

targets so as to ensure it plays its full role in achieving the agreed goal. Caps would be set consistent with such new international obligations.

- The economic implications associated with various levels of national scheme caps, including the carbon price ***[Part 2, clause 14(5)(c)(iii)]***. The White Paper stated that all of the design elements of the scheme were to take into account the criteria of minimising implementation risks and the implications for the competitiveness of traded and non-traded industries. The economic implications of scheme caps have a bearing on these factors. Different levels of scheme caps will have different economic implications, including on likely carbon prices and/or the flow of funds outside Australia to purchase eligible international units. In addition, judgements about the appropriate level of the cap will take into account the carbon price and economic impacts arising from observing the actual operation of the cap in previous years. The carbon price may be higher or lower than expected as a result of a number of factors. For example, technological developments may mean that economic costs are lower than expected as new unanticipated abatement opportunities come into play. Conversely, some expected abatement opportunities may be more costly due to developments in other markets, such as the price of fuels. It may be appropriate to take these factors into account when judging where within the overall bounds set by the gateway caps should be set, along with the other elements outlined in this clause.

- The extent of actions voluntarily taken by Australian households to reduce Australia's greenhouse gas emissions ***[Part 2, clause 14(5)(c)(iv)]***. Voluntary action to reduce greenhouse gas emissions can help ameliorate the economic implications associated with various levels of national scheme caps, making it more likely that more stringent caps can be set over time.

- Estimations of emissions that are not covered by the Scheme ***[Part 2, clause 14(5)(c)(v)]***. In order to meet national emissions objectives, account may need to be taken of the remainder of emissions that are not covered by the Carbon Pollution Reduction Scheme.

- Such other matters as the Minister considers relevant ***[Part 2, clause 14(5)(c)(vi)]***.

2.20 To provide further guidance to liable entities and participants in the carbon market more generally, national scheme gateways may be prescribed for years beginning on or after 1 July 2015 ***[Part 2, clause 15]***. A gateway is a range, comprising an upper bound and a lower bound of emissions, expressed in terms of tonnes of carbon dioxide equivalent, for a particular year. The Minister is required to take all reasonable steps to ensure that the scheme caps are within the range specified for the relevant year. The factors the Minister will have regard to are the same as those described above in relation to the setting of national scheme caps ***[Part 2, clause 15(4)]***.

2.21 Gateways can be used to indicate longer term possibilities for cap-setting. For example, they could be used to more formally signal a policy intention for Australia to play its full and fair part in any international agreement to deliver global concentrations of greenhouse gases of 450 parts per million or better (in carbon dioxide equivalent terms). The top of the gateway would define the maximum cap for a particular year, which in turn relates to the minimum amount of greenhouse gas abatement that would be required in that year.

2.22 The Minister is required to 'take all reasonable steps' to ensure that the relevant regulations are made ***[Part 1, clauses 14-15]***. This phrase has been adopted because, despite their best endeavours, a Minister cannot ensure that regulations are made and not disallowed.

Emissions units

2.23 Emissions units are addressed in Part 4 of the draft bill. It commences with a simplified outline ***[Part 4, Division 1, clause 82].***

2.24 The units which can be used for surrender are 'eligible emissions units'. This phrase is defined to mean Australian emissions units and eligible international emissions units ***[Part 1, clause 5, definition of 'eligible emissions unit']***.

2.25 The inclusion of eligible international emissions units provides for the Scheme to link to international markets. This is achieved by accepting international emissions units for surrender, referred to as importing. There will be no limit on the number of eligible international emissions units that can be used for surrender to meet obligations under the Scheme.

2.26 A unit is an eligible international emissions unit ***[Part 1, clause 5, definition of 'eligible international emissions unit']*** if it is:

- A certified emission reduction other than a long-term or temporary certified emission reduction
- An emission reduction unit
- A removal unit
- A prescribed unit issued in accordance with the Kyoto rules
- A non-Kyoto international emissions unit (which must be prescribed in regulations).

2.27 Consistent with the Government's policy, not all Kyoto units (explained below) will be able to be surrendered initially. For example assigned amount units and temporary and long-term certified emission reductions are not included in the definition of an eligible international emissions unit. However, the definition of eligible international emissions unit allows for regulations to prescribe additional types of units that are issued in accordance with the Kyoto rules. For example, should the Kyoto Protocol rules include a new type of unit in the future, this provision will allow for any such unit to be prescribed as an eligible international unit without an amendment to the Act.

2.28 The definition of eligible international emissions unit also includes a non-Kyoto international emissions unit (discussed below), which is defined as a prescribed unit issued in accordance with an international agreement (other than the Kyoto Protocol); or a prescribed unit issued outside Australia under a law of a foreign country ***[Part 1, clause 5, definition of 'non-Kyoto international emissions unit']***. This allows for regulations to add to the types of international emissions units that can be surrendered without an amendment to the Act.

2.29 Provisions that allow for the future sale and transfer of Australian emissions units to foreign registries (export) will be included in the final bill. The Government's policy is that export would not be provided for in the initial years of the scheme and that it would give the market five years' notice of a decision to allow for export. An exception to this general policy is to be made for bilateral links where an independent review finds that establishing the bilateral link will not have a significant impact on the unit charge, where the Minister may decide to waive or shorten the notice period. The policy also indicated that, when allowed, the outgoing transfer of units would be achieved either by allowing unit holders to convert the unit into an international emissions unit such as a Kyoto unit which could then be transferred to a foreign registry; or by the direct transfer of a unit to a foreign registry. The final provisions will be consistent with this policy.

Australian emissions units

Issue, identification number and vintages

2.30 Australian emissions units will be issued by the Authority on behalf of the Commonwealth ***[Part 4, Division 2, clause 83]***. To hold an Australian emissions unit, the person must have a Registry account. Units are issued by the Authority making an entry for the unit in the person's Registry account ***[Part 4, Division 2, clause 87]***. The unit will thus be represented by an electronic entry in the Registry, rather than by a paper certificate.

2.31 Each Australian emissions unit will have a unique number known as the identification number ***[Part 4, Division 2, clause 84]***. The entry by the Authority in an account when issuing a unit consists of the identification number of the unit ***[Part 4, Division 2, clause 87(2)]***.

2.32 Each Australian emissions unit will have a certain vintage year. This will be the last four digits of the identification number. The vintage year of the unit is the financial year that ends on 30 June in that calendar year. For example, if the last four digits of an Australian emissions unit identification number are 2011, the vintage year of the unit is the financial year beginning 1 July 2010 and ending on 30 June 2011 ***[Part 4, Division 2, clause 85]***.

2.33 The Authority may issue an Australian emissions unit with a particular vintage year at any time before the end of 15 December following the vintage year ***[Part 4, Division 2, clause 86]***. For example, the Authority may, at any time before the end of 15 December 2011, issue an Australian emission unit with the vintage year that ends on 30 June 2011. This will allow for an auction of units in the interval between the end of the relevant financial year and 15 December, the final date for surrender.

2.34 Australian emissions units do not have a 'use by' date. They can be used for surrender in their vintage year and thereafter. This is referred to as 'banking'. There is limited capacity to surrender Australian emissions units which are of the following vintage year ('borrowing') ***[Part 6, Division 2, clause 129(4)]***. The purpose of allowing banking and limited borrowing is to allow liable entities to shift the timing of their emissions and abatement activities to reduce their costs. It will also have the effect of smoothing the unit price over time. More details, the timetable and process for surrender are described in Chapter 8 of this commentary.

Circumstances in which they can be issued

2.35 Australian emissions units can only be issued in the following circumstances:

- As the result of an auction conducted by the Authority
- In accordance with the provisions relating to the issue of units for a fixed charge
- In accordance with the emissions-intensive trade-exposed assistance program
- In accordance with Part 9 which relates to coal-fired electricity generation
- In accordance with Part 10 which relates to reforestation
- In accordance with Part 11 which relates to destruction of synthetic greenhouse gas.

[Part 4, Division 2, clause 88]

2.36 Details about the procedure for allocation in each of these circumstances are provided in Chapter 3 to 7 of this commentary.

2.37 Australian emission units for a particular vintage cannot be issued unless there is a national scheme cap number for the vintage year ***[Part 4, Division 2, clause 92]***. Also the Authority must ensure that the sum of Australia emissions units issued at auction, added to those issued in accordance with the emissions–intensive trade-exposed assistance programme and in accordance with provision for assistance to coal fired electricity generators, does not exceed the scheme cap ***[Part 4, Division 2, clause 93]***.

Characteristics of Australian emissions units.

2.38 An Australian emissions unit is personal property and, subject to the relevant provisions in the draft bill, transmissible by assignment, by will and by operation of law ***[Part 4, Division 2, clause 94].***

2.39 The Government's policy intent in adopting this approach in the draft bill is to reduce uncertainty for holders of Australian emissions units, and promote market confidence in and development of the carbon market.

2.40 The draft bill is not intended to prevent the creation of equitable interests in Australian emissions units or the taking of security over them.

2.41 Further consideration will be given in the period following release of the exposure draft to the mechanisms for taking security over them.

2.42 Once an Australian emissions unit is surrendered, it is cancelled ***[Part 6, Division 2, clause 129(10)]***. It is also cancelled if it is offered for voluntary cancellation ***[Part 14, clause 282(3)]***. Some units are cancelled following relinquishment ***[Part 15, Division 2, clause 286]***. Surrender, relinquishment and voluntary cancellation are explained in greater detail in Chapter 8 of this commentary.

Transfer and transmission of Australian emissions units

2.43 The concept of transfer of an Australian emissions unit is described. In general, it consists of the removal of an entry for the unit from the first account and making an entry for the unit in the second account ***[Part 4, Division 2, clause 95].***

2.44 There is provision for:

- The transfer of Australian emissions units between accounts within the Australian National Registry, in the name of the same person ***[Part 4, Division 2, clause 98]***
- Transmission of Australian emissions units by assignment ***[Part 4, Division 2, clause 96]***
- Transmission of Australian emissions units by operation of law ***[Part 4, Division 2, clause 97].***

2.45 At its simplest, a transfer is initiated by an electronic instruction from the transferor transmitted to the Authority which removes the entry for the unit from one account and makes an entry for that unit in another account.

2.46 Transmissions by operation of law bring additional issues. An example is transmission of a unit to a person as the trustee of a deceased person's estate. In this situation it is the transferee which needs to establish evidence of transmission and, if necessary, open a Registry account ***[Part 4, Division 2, clause 97].***

Kyoto units

2.47 The draft bill provides for the recognition in Australian legislation of the emissions units created under the Kyoto Protocol, and sets out how these units can be issued and transferred ***[Part 4, Division 3].*** The provisions relating to Kyoto units have been drafted to ensure the Australian legislation is consistent with the Kyoto Protocol rules.

The Kyoto rules

2.48 The draft bill defines the Kyoto rules to mean:

- the Kyoto Protocol
- a decision of the Meeting of the Kyoto Parties
- a standard or other instrument adopted by the Meeting of the Kyoto Parties for a purpose relating to:
  - the Kyoto Protocol

  or

  - a decision of the Meeting of the Kyoto Parties

  or
- a prescribed instrument that relates to:
  - the Kyoto Protocol

  or

  - a decision of the Meeting of the Kyoto Parties

[Part 1, clause 5, definition of 'Kyoto rules']

2.49 Defining the Kyoto rules in this way allows for all the relevant elements of the Kyoto Protocol framework to be adopted for various purposes in the bill. The definition of Kyoto rules is also intended to allow the flexibility for the legislative framework to accommodate new decisions and standards without necessarily requiring an amendment to the Act.

2.50 As the Kyoto Protocol itself only provides for the overarching framework with relevant decisions made by the Meeting of the Kyoto Parties providing the detail, the definition of Kyoto rules also encompasses those decisions. For some purposes the Meeting of the Kyoto Parties has adopted a standard or other instrument which governs the implementation of the Kyoto Protocol. For example, the data exchange standards govern the operation of the international transaction log. Therefore, the definition of Kyoto rules also includes any such standards or instruments. The definition also allows for regulations to identify any other instruments that relate to the Kyoto Protocol or a decision of the Meeting of the Kyoto Parties to be considered part of the Kyoto rules.

Kyoto units in the Australian registry

2.51 There is a distinction in the draft bill between the provisions relating to holding and transferring Kyoto units and those relating to surrender of eligible international units. While some types of Kyoto units are eligible international emissions units and can be surrendered, others such as assigned amount units and temporary and long-term certified emission reductions, are not eligible international units and therefore cannot be surrendered. Regardless, all Kyoto units will be able to be held and transferred in the Australian Registry.

2.52 A Kyoto unit is defined for the purposes of the draft bill to mean an assigned amount unit, a certified emission reduction, an emission reduction unit, a removal unit or a prescribed unit issued in accordance with the Kyoto rules ***[Part 1, clause 5, definition of 'Kyoto unit']***. The last element of this definition allows for the recognition of a new type of Kyoto unit that could be adopted in the future without an amendment to the Act.

2.53 Each type of Kyoto unit is also defined for the purpose of the draft bill. The form of each definition refers to the relevant provisions of the Kyoto rules.

2.54 An assigned amount unit is defined to be an assigned amount unit issued in accordance with the relevant provisions of the Kyoto rules. ***[Part 1, clause 5, definition of 'assigned amount unit']*** By way of background, assigned amount units are issued by an Annex I country (a developed country with a target) to the Kyoto Protocol on the basis of its assigned amount pursuant to Articles 3.7 and 3.8 of the Kyoto Protocol (for example, Australia will issue assigned amount units equal to its target - 108% of 1990 emissions for the five year period, 2008-2012). As assigned amount units can be issued by any Annex I country, the definition indicates that for the purposes of the draft bill it is immaterial whether the unit was issued in or out of Australia. This is included in the definition to make it clear that the general rule in s 21(1)(b) of the *Acts Interpretation Act 1901* does not apply. That rule is that 'references to localities jurisdictions and other matters and things shall be construed as references to such localities jurisdictions and other matters and things in and of the Commonwealth…'

2.55 A certified emission reduction is defined to be a certified emission reduction issued outside Australia in accordance with the relevant provision of the Kyoto rules ***[Part 1, clause 5, definition of 'certified emission reduction']***. By way of background, certified emission reductions are generated from clean development mechanism projects under Article 12 of the Kyoto Protocol. The clean development mechanism allows Annex I countries like Australia to implement emission reduction projects

in developing countries to receive certified emission reductions and use these towards meeting their Kyoto target.

2.56 Unlike emission reductions from other types of clean development mechanism projects, those arising from afforestation or reforestation activities receive either a temporary certified emission reduction or a long-term certified emission reduction. These units have a limited life, fewer than two commitment periods for temporary certified emission reductions and between 20 and 60 years for long-term certified emission reductions. These Kyoto units are also defined in the draft bill by reference to the relevant provisions of the Kyoto rules ***[Part 1, clause 5, definition of 'certified emission reduction']***.

2.57 A removal unit is defined to be a removal unit issued in accordance with the relevant provisions of the Kyoto rules. It is immaterial whether the unit was issued in or out of Australia ***[Part 1, clause 5, definition of 'removal unit']***. Removal units are issued by an Annex I country on the basis of land use, land-use change and forestry activities under Articles 3.3 and 3.4 of the Kyoto Protocol.

2.58 An emission reduction unit is defined to be an emission reduction unit issued in accordance with the relevant provisions of the Kyoto rules. It is immaterial whether the unit was issued in or out of Australia ***[Part 1, clause 5, definition of 'emission reduction unit'].*** They are generated by joint implementation projects under Article 6 of the Kyoto Protocol, where an Annex I country like Australia can implement a project in the territory of another Annex I country and count the resulting emission reduction units towards meeting its own Kyoto target. Emission reduction units can be generated either in another Annex I country or in Australia. However, Australia will not host joint implementation projects in the first commitment period, so it is not expected that any emission reduction units will be issued in Australia during this period. A decision will be made in regards to any potential for joint implementation projects in 2013 when decisions are made about the scope for offsets more generally.

2.59 Kyoto units only exist within the international electronic registry system established by the Kyoto rules. Each Kyoto unit has a unique serial number within that electronic registry system that provides the relevant detail of the unit (such as its type, commitment period, country of origin and its sequence number) and allows for the unit to be tracked throughout the registry system. Consistent with the Kyoto rules, the entry of a Kyoto unit in a Registry account consists of the serial number ***[Part 4, Division 3, clause 104]***.

Issue of Australia's assigned amount units

2.60 As an Annex I country, under the Kyoto Protocol, Australia is allocated Kyoto units called 'assigned amount units' on the basis of its initial assigned amount, where each assigned amount unit signifies an allowance to emit one tonne of CO_2-e. Australia's calculation of its initial assigned amount, and the method by which it is calculated, is set out in Australia's initial report under the Kyoto Protocol. After the initial report has been reviewed by the Kyoto Protocol expert review team and any questions of implementation have been resolved, Australia's initial assigned amount will be recorded in the UNFCCC Secretariat's compilation and accounting database and provided to the international transaction log.

2.61 Australia must then, before any transactions takes place for the relevant commitment period, issue a quantity of assigned amount units equivalent to its initial assigned amount in its national registry.

2.62 The draft bill provides for the issue of Australia's assigned amount units for a commitment period ***[Part 4, Division 3, clause 105]***. Under this provision, the Minister may direct the Authority to issue to the Commonwealth, in accordance with the Kyoto rules, a specified number of assigned amount units for a specified commitment period. The Authority must comply where such a direction is given and will issue an assigned amount unit by making an entry for the unit in a Commonwealth holding account in the Registry.

2.63 It is possible that Australia's assigned amount units for the first commitment period will be issued under the Commonwealth's executive power before the passing of the legislation. The draft bill is explicit that it does not affect the validity of the issue of any such units. ***[Part 4, Division 3, clause 105(5)]***

Issue of Australia's removal units

2.64 Under the Kyoto Protocol, removal units are issued in relation to net removals of greenhouse gases by Article 3.3 activities (afforestation, reforestation and deforestation). Australia has elected to report and publish annual estimates of emissions and removals from activities identified under Article 3.3. This decision is fixed for the first commitment period and means that Australia must issue or cancel units (as appropriate) for the relevant activities on an annual basis. If net removals do occur, it is expected that Australia will issue a quantity of removal units in its national registry equivalent to those removals.

2.65 The draft bill provides for the issue of Australia's removal units in the Registry ***[Part 4, Division 3, clause 106]***. Under this provision, the

Minister may direct the Authority to issue to the Commonwealth, in accordance with the Kyoto rules, a specified number of removal units. The Authority must comply with any such direction. The Authority will issue a removal unit by making an entry for the unit in a Commonwealth holding account in the Registry.

Transfers of Kyoto units

2.66 The Kyoto rules allow for Kyoto units to be transferred within the international electronic registry system. The electronic registry system comprises of the various national registries of Kyoto countries; the clean development mechanism registry in which certified emission reductions can be issued; and the international transaction log that allows for inter-country transfers of units. Within each of the national registries, Kyoto units can be transferred between different accounts.

2.67 The draft bill provides for the meaning of 'transfer' in relation to different types of transfers of Kyoto units ***[Part 4, Division 3, clause 107]***. There are several different types of transfers that have been identified. In each case a 'transfer' of a Kyoto unit will consist of the removal of the entry of the unit from the initial account and an entry for the unit in the receiving account.

2.68 These four different types of transfers allow for transfer between any of the account types in the national Registry. (Chapter 10 of this commentary discusses the different types of Registry accounts). For example a transfer can be: between holding accounts including a Commonwealth holding account; between a holding account and a Commonwealth cancellation account; and between a Commonwealth holding account and a Commonwealth retirement account.

2.69 The Commonwealth will need to transfer Kyoto units between the Commonwealth accounts. The same transfer arrangements will apply where it is the Commonwealth that wishes to transfer Kyoto units. In this case the draft bill provides for the Minister to give an instruction to the Authority ***[Part 4, Division 3, clauses 108(5) and 109(7)].***

2.70 Regulations can be made to give effect to the Kyoto rules in relation to: transfer of a Kyoto unit from a Registry account to a foreign account; or from a foreign account to a Registry account or the transfer of a Kyoto unit from a Registry account to a Commonwealth Registry account or the issue of a Kyoto units ***[Part 4, Division 3, clause 112(1)]***. This is intended to give full effect to the relevant Kyoto rules (including as those rules change from time to time), with regulations providing the detail for the administration of the Registry as it relates to Kyoto units. The regulations may prevent, restrict or limit:

- the transfer of Kyoto units from a Registry account to a foreign or voluntary cancellation account
- the transfer of Kyoto units from a foreign to a Registry account.

[Part 4, Division 3, clause 112(2)]

Domestic transfer of Kyoto units

2.71 If a person is a holder of a Kyoto unit they may instruct the Authority to transfer the unit within the Australian Registry, this is considered a domestic transfer ***[Part 4, Division 3, clause 108]***. The instruction to transfer will be by electronic notice and will set out the account number of the account where the Kyoto unit is held; the account number of the Registry account to which the unit is being transferred; and other information as specified in regulations. The regulations may specify additional information consistent with the administrative requirements of the Registry.

2.72 The Authority must give effect to the transfer instruction unless that would breach any regulations made to give effect to the Kyoto rules or the management of the commitment period reserve ***[Part 4, Division 4, clauses 108(3), 112, 114]***.

International transfers of Kyoto units

2.73 Under the Kyoto rules, Australia must satisfy a set of eligibility requirements in order to participate in international emissions trading. If Australia does not satisfy the set of eligibility requirements no transfers of Kyoto units will be allowed between the Australian Registry and a foreign registry. The international transaction log will block any such transfers where Australia does not satisfy the eligibility requirements. Therefore, the ability to transfer Kyoto units from a foreign registry to an account within the Australian Registry and the ability to transfer Kyoto units from the Australian Registry to a foreign registry are dependent on Australia satisfying the eligibility requirements.

2.74 Under the draft bill, if satisfied that Australia is in compliance with those eligibility requirements, the Minister must make a written declaration to that effect. The Minister must, in writing, revoke such a declaration if the Minister is no longer satisfied that Australia is in compliance with those requirements ***[Part 4, Division 3, clause 111]***. Neither the instrument of declaration nor revocation is a legislative instrument ***[Part 4, Division 3, clause 111(3)]***. The policy reason for this is that the Minister does not have discretion as to whether Australia is eligible or not. The enforcement branch of the compliance committee under the Kyoto

Protocol framework is responsible for determining whether an Annex I Party is not in compliance with the eligibility requirements. In practice, the UNFCCC secretariat maintains a list of Parties that meet the eligibility requirements and of those Parties that have been suspended on their website.

2.75 Kyoto units can be transferred from an account in the Australian Registry to a foreign registry, referred to as an outgoing international transfer ***[Part 4, Division 3, clause 109]***. A transfer would only be possible where there is a declaration in force that Australia has met the emissions trading eligibility requirements discussed above ***[Part 4, Division 3, clause 111]***.

2.76 A holder of a Kyoto unit would instruct the Authority by electronic notification to transfer the Kyoto unit from the relevant Registry account to either a foreign account kept by another person or a foreign account kept by that person. Similar to domestic transfers the notification will need to specify the account number from which the units are to be transfer and any other information as specified in regulations.

2.77 The specific process for administering outgoing international transfers will be detailed in the regulations made to give effect to the Kyoto rules. The regulations may require the Authority to remove the entry for the unit from the relevant Registry account ***[Part 4, Division 3, clause 109(4)].*** This would be consistent with the normal process of the international registry system which is designed to ensure that units can be appropriately transferred and tracked between different accounts and national registries.

2.78 The Authority will not give effect to the outgoing international transfer if the transfer would breach regulations made for the purposes of the Kyoto rules ***[Part 4, Division 3, clause 112 and 109(3)(a)(i)]*** (discussed above).

2.79 Similarly, the Authority will not give effect to the outgoing international transfer if the transfer would be in breach of the regulations made to manage the commitment period reserve ***[Part 4, Division 3, clause 114 and 109(3)(a)(ii)]***. By way of background, in order to address concerns that Annex I Parties could oversell units and subsequently be unable to meet their own Kyoto target, each Kyoto Party is required to hold a minimum level of Kyoto units in its national registry called the commitment period reserve. If the transfer of a Kyoto unit from the national registry would result in an infringement of the commitment period reserve, the international transaction log will reject the entire transfer and direct the Authority to terminate the transfer. It is intended that regulations will outline the procedures and measures to manage Australia's commitment period reserve.

2.80 Kyoto units can be transferred from a foreign registry to an account in the Australian Registry, referred to as an incoming international transfer ***[Part 4, Division 3, clause 110]***. A transfer would only be allowed where there is a declaration in force that Australia has met the emissions trading eligibility requirements under ***[Part 4, Division 3, clause 111]***.

2.81 In practice, an incoming international transfer is going to be initiated by a foreign registry. The foreign registry will notify the international transaction log, which will verify the transaction. The international transaction log will then notify the Authority of an incoming transfer of a Kyoto unit. Accordingly, it is the receipt of an instruction from the international transaction log by the Authority which is the trigger for an incoming international transfer under the draft bill ***[Part 4, Division 3, clause 110(1)(b)]***.

2.82 An incoming international transfer will only be allowed where the Kyoto unit is not specified in the regulations as a unit that cannot be transferred to a Registry account ***[Part 4, Division 3, clause 110(1)(c)]***. Under section 13(3) of the *Legislative Instruments Act 2003,* regulations can be made which specify a class or classes of Kyoto units. This means that regulations can exclude certain Kyoto units from being transferred into the Registry. These regulations will not affect units already in the Registry.

2.83 This gives effect to the Government's policy position that it would retain the right to exclude any type of Kyoto unit from being transferred into the Registry. Currently there is no specific class of Kyoto unit that has been identified for exclusion by regulation. The regulation-making power provides flexibility to respond to future circumstances without the need for an amendment. For example, the White Paper stated that it is important to retain the right to disallow a certain type of international unit for compliance in the scheme at any time to ensure the environmental integrity of the Scheme. To avoid disadvantaging liable entities who had bought those units in good faith, they would be able to use it for compliance in that compliance year but not thereafter. This policy is addressed in the surrender provisions ***[Part 6, Division 2, clause 129(7)]***. However, this potentially raises concerns that the Scheme could be open to a 'flood' of compromised units. Retaining the right to disallow that type of unit from entering the Australian registry by specifying it in regulations would stop such a scenario.

2.84 Another example where this regulation-making power may be used would be in the event the Kyoto rules changed in a way that could potentially result in a liability on the Commonwealth associated with the treatment of Kyoto units held in its registry. The regulations could specify that such units could no longer enter the Registry.

2.85 An incoming international transfer will also only be allowed where the transfer would not breach regulations made to give effect to the Kyoto rules which are discussed above ***[Part 4, Division 3, clause 112]***.

2.86 Provided these requirements are met the Authority must make an entry for the Kyoto unit in the relevant Registry account. However the Authority may refuse to make an entry if it has reasonable ground to suspect that the instruction is fraudulent ***[Part 4, Division 3, clause 110(2)]***.

Carry-over restrictions

2.87 Under the Kyoto Protocol, an Annex I Party may carry over to a subsequent commitment period (that is, it may bank) certain Kyoto units that have not been retired for that commitment period, cancelled or transferred to the replacement account. Under the current Kyoto rules, the extent to which the Party can carry over the units differs depending on the kind of units involved:

- Emission reduction units (not converted from removal units) can be carried over up to a maximum of 2.5% of the country's initial assigned amount
- Certified emission reductions can be carried over up to a maximum of 2.5% of the country's initial assigned amount
- Assigned amount units can be carried over without restriction
- Removal units, emission reduction units converted from removal units, temporary certified emission reductions and long-term certified emission reductions cannot be carried over.

2.88 Any Kyoto units that are not carried-over must be transferred to the mandatory cancellation account.

2.89 The draft bill provides for regulations to be made detailing arrangements for the carry over of Kyoto units ***[Part 4, Division 3, clause 113]***. It is intended that the regulations will identify the units that can be carried over and any limits or restrictions that are specified; identify the Kyoto units that cannot be carried over; set out the procedures for the carry-over; and set out any prohibition on surrender. The regulations will also provide for the Authority to transfer to the mandatory cancellation account those Kyoto units that are not carried over.

Temporary certified emission reductions and long-term certified emission reductions

2.90 As discussed above, temporary certified emission reductions and long-term emission reductions generated from forestry-based clean development mechanism projects have a limited life after which they expire. Hence these units are non-permanent.

2.91 Temporary certified emission reductions expire at the end of the commitment period after the one in which they were issued, while long-term certified emission reductions expire at the end of the crediting period of the project. While these certified emission reductions cannot be surrendered for compliance under the draft bill, account holders may transfer and hold these units within the Australian Registry.

2.92 Where either a temporary certified emission reduction or a long-term certified emission reduction is in a person's Registry account when it expires, the Authority must, in accordance with the regulations, transfer the temporary or long-term certified emission reduction to a voluntary cancellation account ***[Part 4, Division 3, clause 115]***.

2.93 The Kyoto rules require replacement of long-term certified emission reductions in certain circumstances. In brief, because long-term certified emission reductions are valid for long periods, the projects that generate them must be re-certified by an independent auditor every 5 years to demonstrate that the emission removals have occurred. When a certification report indicates that the greenhouse gas removals achieved by a project have been reversed since the last certification (for example where the trees are cut down), the Kyoto rules require replacement of the affected long-term certified emission reductions. Replacement is also required if the Clean Development Mechanism Executive Board determines that the required certification report has not been submitted.

2.94 The draft bill provides for the making of regulations to provide for the requirements for a person to replace long-term certified emission reductions in their Registry account ***[Part 3, Division 3, clause 116]***. The Authority will be required to transfer long-term certified emission reductions to the voluntary cancellation account in the event that long-term certified emission reductions are not replaced in accordance with the regulations. The meaning of 'replacement' of a long-term certified emission reduction is set in clause 116(3).

Non-Kyoto international emissions units

2.95 As discussed above, a non-Kyoto international emissions unit is defined to mean: a prescribed unit issued in accordance with an

international agreement (other than the Kyoto Protocol); or a prescribed unit issued outside Australia under a law of a foreign country ***[Part 1, clause 5, definition of 'non-Kyoto international emissions unit']***. A unit would only be prescribed as a non-Kyoto international emissions unit where the intention is to add to the types of international units that can be used for surrender. That is, all non-Kyoto international emissions units will also come within the definition of 'eligible international emissions units' ***[Part 1, clause 5, definition of 'eligible international emissions units']***.

2.96 This is consistent with the policy which allows for the addition to the types of international units that can be used for compliance, where:

- the addition does not compromise the environmental integrity of the Scheme
- the addition is consistent with the objective of the scheme, including Australia's international objectives
- there has been consultation with stakeholders and analysis of the expected impact on the unit price by an independent review. For example, if a bilateral link were established with another country's scheme the regulations would allow for the unit of the other scheme to be accepted in the Scheme.

2.97 It is also consistent with the policy in relation to pursuing bilateral links with the schemes of other countries, such as New Zealand. These will be considered on a case-by-case basis. For example, if a bilateral link were established, the New Zealand unit would be prescribed as a non-Kyoto international emissions unit and then Australian liable entities would be able to surrender those units.

2.98 Like Australian emissions units and Kyoto units, an entry for a non-Kyoto international emissions unit on the Registry will consist of the serial number of the unit ***[Part 4, Division 4, clause 117]***.

2.99 As in the case of Kyoto units, the regulations may prohibit the surrender of non-Kyoto international emissions units ***[Part 4, Division 4, clause 122].***

2.100 The draft bill provides a framework with the detailed arrangements for transfers of non-Kyoto international emissions units to be specified in regulations ***[Part 4, Division 4, clause 123]***. This allows the transfer arrangements of such units to be in accordance with, for example, any associated treaty or agreement.

Transfers of non-Kyoto international emissions units

2.101 The draft bill provides for the meaning of 'transfer' in relation to different types of transfers of non-Kyoto international emissions units in the Registry ***[Part 4, Division 4, clause 118]***. As with other emissions units, a transfer will involve the removal of the entry of the unit from the registry account of the person initiating the transfer and the making of an entry for the unit in the receiving registry account. Several different types of transfer have been identified. The unit can be transferred from a registry account to a registry account of another person; from the registry account to another registry account owned by the same person; from the registry account to an account in a foreign registry owned by the same person; and from an account in a foreign registry to an account in the Australian registry.

2.102 It is possible that the Commonwealth may wish to transfer non-Kyoto international emissions units. If so, the Minister has the power to instruct the Authority to undertake the transfer ***[Part 4, Division 4, clauses 119(5) and 120(7)]***. Otherwise the general provisions for transfers would apply.

2.103 A person who holds a non-Kyoto international emissions unit can instruct the Authority to transfer the unit to an account kept by another person or to another account kept by the same person within the Registry ***[Part 4, Division 4, clause 119]***. The instruction will be via electronic notification and will include the account number of the originating account and the account number of the receiving account and any other information that is specified in regulations governing the administration of the registry.

2.104 The provision allows for conditions relating to domestic transfer of non-Kyoto units to be provided for in regulations. If the Authority receives an instruction and any such conditions are satisfied then the Authority must give effect to the transfer.

2.105 Non-Kyoto international emissions units can be transferred from an account in the Australian registry to an account in a foreign registry, referred to as an outgoing international transfer of non-Kyoto international emissions units ***[Part 4, Division 4, clause 120]***. Again the transfer could be to an account kept by another person or kept by the same person, with the instruction via electronic notification and containing the relevant account details and other information.

2.106 Regulations may detail any conditions that may apply to outgoing international transfers of non-Kyoto international emissions units. The administrative arrangements for giving effect to the transfer would also be specified in regulations ***[Part 4, Division 4, clause 123]***.

2.107 Non-Kyoto international emissions units can be transferred from a foreign account to an account in the Registry, referred to as an incoming international transfer of non-Kyoto international emissions unit ***[Part 4, Division 4, clause 121]***. In this case the Authority would receive an instruction from a foreign account and, where the conditions as specified in the regulations are met, the Authority would make an entry for the non-Kyoto international emissions unit in the nominated account in the Australian registry.

2.108 However the Authority may refuse to affect the transfer if it has reasonable grounds to suspect that the instruction was fraudulent ***[Part 4, Division 4, clause 121(2)]***.

Chapter 3
Allocation of units – introduction, auction and fixed charge units

Outline of chapter

3.1 This chapter introduces the various ways in which Australian emissions units are to be allocated and describes two of these: auctions and the issue of units for a fixed charge.

Context of amendments

National target and scheme caps

3.2 As indicated in the General Outline, the Government has decided to take action towards meeting Australia's targets of reducing greenhouse gas emissions to 60% below 2000 levels by 2050 and reducing greenhouse gas emissions to between 5% and 15% below 2000 levels by 2020, and to do this in a flexible and cost-effective way. These national targets are set out in one of the objects of the Scheme specified in the draft bill ***[Part 1, clause 3]***.

3.3 Scheme caps will be set to support national emissions targets and Australia's international obligations. Scheme caps will be lower than the emissions path required to meet the national targets because some emissions sources are not covered by the Scheme (primarily, agricultural and deforestation emissions) and direct emissions from facilities are only covered if they exceed specified thresholds (usually 25,000 tonnes of carbon dioxide equivalence per year).

3.4 Scheme cap numbers will be specified in regulations ***[Part 2, clause 14]***.

3.5 Further discussion about national scheme caps and gateways is included in Chapter 2 of this commentary.

Issue of Australian emissions units

3.6 The circumstances in which the Authority may issue Australian emissions units are described ***[Part 4, Division 2, clause 88]***. They are:

- as the result of an auction conducted by the Authority (described in more detail in this chapter)
- in accordance with the provisions governing the issue of units at a fixed charge (described in more detail in this chapter)
- in accordance with the emissions-intensive trade-exposed assistance program (see Chapter 4)
- in accordance with the provisions regarding coal-fired electricity generation assistance (see Chapter 5)
- for reforestation (see Chapter 6)

or

- for the destruction of synthetic greenhouse gas (see Chapter 7).

3.7 The Authority must not issue an Australian emissions unit with a particular vintage unless there is a national scheme cap number for that vintage year ***[Part 4, Division 2, clause 92]***. (Consistently, there is no obligation to surrender unless there is a national scheme cap number for the relevant financial year ***[Part 6, Division 4, clause 132]***.)

3.8 The number of units offered for issue at auctions and issued in accordance with the emissions-intensive trade-exposed assistance program and the provisions regarding coal-fired electricity generation assistance must equal the scheme cap for the particular year ***[Part 4, Division 2, clause 93]***.

Summary

Auctions

3.9 The Government has decided that a large proportion of Australian emissions units will be auctioned. The primary policy objectives of the auction are to promote allocative efficiency and efficient price discovery. Auctions will also raise revenue that can be used for

other policy objectives, such as providing assistance to households and business, although this is not a primary objective.

3.10 The provisions relating to auctions are in Part 4, Division 2 Subdivision C, clauses 99-103 of the draft bill.

3.11 It is the Government's policy that allocations will, over the longer term, progressively move towards 100% auctioning over time, subject to the provision of transitional assistance for emissions-intensive trade-exposed industries and compensation for coal-fired electricity generation.

3.12 The Authority will be required to publish information about the auction results to assist Scheme participants and financial market analysts to identify and understand the overall supply and demand conditions for units, allowing efficient price discovery ***[Part 12, Division 4, clause 270]***. This is discussed in Chapter 11 of this commentary.

Fixed charge units (Scheme Price Cap)

3.13 The Scheme will have a price cap in the form of access to an unlimited store of additional Australian emissions units, issued at a fixed charge, for the first five financial years. The purpose of the price cap is to set a maximum cost of compliance for liable entities. Liable entities will have the option of purchasing these units before the final surrender date for a particular financial year. These units cannot be traded or banked for future use.

3.14 The amount of the charge for each year is set out in the draft bill ***[Part 4, Division 2, clause 89]***. The Government's intention is to set it high enough so that its probability of use is low, while providing protection against major price shocks. The amount of the charge rises in real terms by 5% per year. The increases in the charges set out in the legislation assume that the inflation rate is 2.5% per year.

3.15 The provisions relating to the issue of Australian emissions units for a fixed charge are Part 4, Division 2, clauses 89-91.

Detailed explanation of new law

Auctions - issue

3.16 The Authority is empowered to issue Australian emissions units through auctions ***[Part 4, Division 2, clause 99]***.

3.17 The detailed policies, procedures and rules for the conduct of auctions will be included in a legislative instrument ***[Part 4, Division 2, clause 103]***.

3.18 The legislative instrument may deal with a range of matters. These include but are not limited to the types of auction, their timing, participants, entry fees, minimum number of units in bids, deposits, guarantees, and the timing and method of payment ***[Part 4, Division 2, clause 103(5)]***.

3.19 The instrument can address the detailed policies, procedures and rules for auctions of units which are to be issued, units which have been relinquished and units issued without charge which have not been transferred by the original recipient to another person.

3.20 Until 1 January 2012, the Minister has the power to make such an instrument. After that date the Authority will have the power to make the instrument ***[Part 4, Division 2, clauses 103(1) – (3)]***.

3.21 The reason for this approach is that preparation and consultation for the initial auctions will need to be undertaken before the Authority is established and fully operational. The Minister will therefore make the initial instrument. The legislative instrument made by the Minister will continue to have effect until it is replaced by an instrument made by the Authority ***[Part 4, Division 2, clause 103(4)]***.

3.22 The initial instrument is expected to reflect the policy positions in the White Paper. These include that:

- auctions will be held 12 times in a financial year
- at least one auction of the year's vintage will be held after the end of the financial year in the lead-up to the final surrender date (15 December)
- the first auction will take place as early as is feasible in 2010, before the start of the Scheme
- four years of vintages will be auctioned in each year (the current vintage plus advance auctions of three future vintages)
- a simultaneous ascending clock auction will be the preferred auction type. In an ascending clock auction, the auctioneer announces a price for a particular quantity of each vintage and bidders reveal the amount they wish to buy at that price. The auctioneer continues to increase the price until the total

demand is equal to or lower than the amount on offer. The process will be carried out simultaneously with different vintages of units

- bidders will have the option to submit proxy bids in 'sealed bid format' for convenience. Proxy bidding allows bidders to submit in advance their demand schedule for units at various prices. The bid is therefore 'sealed' before the auction has even commenced.

3.23 The Authority must not issue a unit as the result of an auction unless the person pays the charge to the Authority on behalf of the Commonwealth ***[Part 4, Division 2, clause 90]***. This avoids the need for the Authority to collect debt owing on units issued following an auction, and lowers the cost of administering the scheme.

3.24 If the charge is taxation within the meaning of section 55 of the Constitution, the charge is not imposed by the draft bill but by the relevant draft charges bill ***[Part 4, Division 2, clause 91]***.

3.25 The relevant draft charges bills are the Carbon Pollution Reduction Scheme (Charges – Excise) Bill 2009, the Carbon Pollution Reduction Scheme (Charges – Customs) Bill 2009 and the Carbon Pollution Reduction Scheme (Charges – General) Bill 2009. There is a separate commentary for each of these draft bills.

Auctions – secondary

3.26 The Authority is also empowered to auction:

- Australian emissions units which have been relinquished in certain situations ***[Part 4, Division 2, clause 100]***

- On behalf of the holder, Australian emissions units issued without charge which have not been transferred by the original recipient to another person ***[Part 4, Division 2, clause 101]***.

3.27 Each of these powers is examined in further detail below.

Auctions of units which have been relinquished

3.28 In certain situations where excess units have been issued, a person can be required to relinquish units, that is, return them to the Commonwealth. These situations are described in Chapter 8 of the commentary. They include situations relating to reforestation, such as the voluntary withdrawal of reforestation projects from the Scheme; the issue

of excess units for emissions-intensive trade-exposed activities that have ceased; and the issue of units as a result of fraudulent conduct by the recipient.

3.29 Where units are relinquished in response to a requirement which is not connected with reforestation or destruction of synthetic greenhouse gases, the units are transferred into the Commonwealth relinquished units account ***[Part 15, Division 2, clause 286(4)]***. These units are then auctioned by the Authority ***[Part 4, Division 2, clause 100]***.

3.30 Units relinquished under the reforestation provisions or in connection with destruction of synthetic greenhouse gases are cancelled ***[Part 15, Division 2, clause 286(3)]***. This is because the units originally issued to the person who relinquished these units were issued above the scheme cap: cancellation ensures that the scheme cap is not artificially inflated.

Auctions of units issued without charge

3.31 Until 31 December 2011, the Authority is empowered to auction units on behalf of persons who had received them without charge in connection with:

- The emissions-intensive trade-exposed assistance program
- Coal-fired electricity generation assistance
- Reforestation
- The destruction of synthetic greenhouse gas.

[Part 4, Division 2, clause 101].

3.32 This will provide a low-risk, low-cost and transparent mechanism that encourages entities receiving a free allocation of units to sell them on the carbon market. This may increase the size of the auction and the amount of units available in the secondary market and reduce hoarding of units.

3.33 Auctions of these units can be combined with auctions of units to be issued for a charge and of certain relinquished units ***[Part 4, Division 2, clause 102]***.

Fixed charge units

3.34 Between 31 October and 15 December following each of the first five financial years of the Scheme's operation, persons with Registry

accounts can apply to acquire from the Authority units at a fixed charge specified in the draft bill ***[Part 4, Division 2, clause 89]***.

3.35 The number of units which can be acquired this way will be limited by the formula:

> The person's emissions number for the vintage year, less the total number of eligible emissions units surrendered by the person in relation to the vintage year ***[Part 4, Division 2, clause 89(2)]***.

3.36 The person is expected to know their emissions number by 31 October, the date by which they are required to report under the National Greenhouse and Energy Reporting Act 2007.

3.37 The final date for acquiring units in this way, 15 December, is the date by which surrender is required.

3.38 The Authority must not issue a unit for a fixed charge unless the person pays the charge to the Authority on behalf of the Commonwealth ***[Part 4, Division 2, clause 90]***.

3.39 The commentary above, which addresses the provisions included to address the possibility that the charge is taxation, applies equally to the fixed charge for units described in this segment.

3.40 Units acquired in this way are taken to have been surrendered immediately after issue ***[Part 4, Division 2, clause 89(5)]***. Units issued for a fixed charge cannot be held over ('banked') for use in compliance in future years. They cannot be transferred or relinquished ***[Part 4, Division 2, clause 89(6)]***.

Chapter 4
Emissions-intensive trade-exposed assistance program

Outline of chapter

4.1 This chapter outlines the effect of the provisions of Part 8 of the draft Carbon Pollution Reduction Scheme Bill 2009 which provide for the emissions-intensive trade-exposed assistance program to be created by the regulations and other provisions associated with that program. Part 8 of the draft bill allows the Government to make regulations which administratively allocate Australian emissions units to persons who conduct emissions-intensive trade-exposed activities. This chapter sets out:

- the context of the policy framework surrounding the emissions-intensive trade-exposed assistance program
- a summary of the core provisions in Part 8
- a detailed description of the individual provisions.

Context

4.2 Australia's adoption of a carbon constraint before other countries may have a significant impact on its emissions-intensive trade-exposed industries. In Chapter 12 of the White Paper the Government outlined its commitment to providing assistance to these industries to reduce the risk of carbon leakage and provide them with some transitional assistance. It committed to do so in a manner that ensures that these industries contribute to the national effort to reduce carbon emissions.

4.3 The Government's proposed emissions-intensive trade-exposed assistance program has been designed to target assistance in as practical and effective a fashion as possible, to support continued growth in emissions-intensive trade-exposed industries and to provide a transparent assistance framework to ensure industry has the clarity and certainty it needs. It will accommodate growth in these industries in a manner that has not been proposed in other cap and trade schemes to date, by directly linking allocations to the production of traded goods by existing and new

entities conducting emissions-intensive trade-exposed activities. The program is based on the expectation that all industries should contribute to the national emissions reduction effort and provides strong incentives for all entities to pursue abatement opportunities.

4.4 Accordingly, the Government's support for emissions-intensive trade-exposed industries will be:

- targeted towards industries that produce traded goods and have the most significant exposure to a carbon price
- directly linked to production and contingent on production continuing in Australia
- balanced against its objectives for non-assisted sectors and households
- consistent with Australia's international trade obligations.

4.5 The assistance will be designed to preserve the incentives for emissions-intensive trade-exposed industries to adjust to a carbon constrained future by:

- providing assistance only in relation to the most emissions intensive activities carried out by an entity
- providing assistance on the same basis to all entities, new and existing, conducting a given activity
- providing assistance on the basis of historical information on the emissions from these activities to ensure that entities have an ongoing incentive to reduce their emissions relative to historical performance.

4.6 The linking of assistance to production levels, and not future emissions, means that the administrative allocation of units will not mute the financial incentives for firms to reduce their emissions. The proposed assistance framework does not reduce the number of units a firm needs to surrender each year in relation to its emissions. Firms conducting emissions-intensive trade-exposed activities, like all other firms in the economy, will therefore retain the incentive to pursue all abatement opportunities that are cost effective at the carbon price. In economic terms, this follows because the opportunity cost of each Australian emissions unit to a firm is the same whether it is freely allocated to the firm or purchased by the firm (either at auction or through the market).

4.7 Assistance will be provided to entities that conduct emissions-intensive trade-exposed activities in the form of an administrative allocation of Australian emissions units at the beginning of each compliance period. The assistance will be provided on an activity basis to ensure that it is well targeted and is equitably distributed within and across industries. The assistance will be provided in relation to the following:

- the direct emissions associated with an activity for which a Carbon Pollution Reduction Scheme (the Scheme) obligation will be incurred
- the emissions associated with the use of steam by an activity
- the cost increase associated with the use of electricity by an activity, which is assessed as resulting from the introduction of the Scheme
- the cost increase related to the upstream emissions from the extraction, processing and transportation of natural gas and its components, such as ethane and methane, used as feedstock by an activity.

4.8 The Government will target assistance to activities that are trade-exposed and emissions-intensive. As outlined in the White Paper:

- Trade-exposure is to be assessed in relation to trade shares being greater than 10 % in any one of the years 2004-05, 2005–06, 2006–07 or 2007–08 or there being a demonstrated lack of capacity to pass through costs due to the potential for international competition.
- Emissions-intensity is to be assessed in relation to whether the industry-wide weighted average emissions intensity of an activity is above a threshold of:
  - 1000 tonnes of carbon dioxide equivalent (CO2-e) per million dollars of revenue

  or

  - 3000 tonnes of carbon dioxide equivalent (CO2-e) per million dollars of value added.

4.9 To determine which activities are eligible for assistance under the emissions-intensive trade-exposed program and should be listed in the Regulations, on 18 February 2009 the Government released a call for a range of industry information in its Guidance Paper: *Assessment of*

Activities for the Purposes of Emissions-Intensive Trade-Exposed Assistance Program. Entities will be required to have this information independently audited. This information will help the Government make an informed decision on the eligibility of an activity for emission-intensive trade-exposed assistance and the rate of assistance provided to the activity.

4.10 In making its decision on the eligibility of activities and the allocative baselines for eligible activities, the Government will consider, in addition to data supplied by entities, publicly available information on pricing, trade and emissions intensity from Australian and international sources.

4.11 The emissions-intensive trade-exposed assistance program will require all entities conducting activities to bear a proportion of the carbon cost they face and provide assistance at two different rates, reflecting the need to provide relatively more assistance to relatively more emissions-intensive activities in order to reduce the likelihood of carbon leakage.

4.12 Initial assistance to eligible activities will be set in the Regulations at:

- 90% of the allocative baseline for activities that have an emissions intensity above 2000 t CO2-e/$million revenue or 6000 t CO2-e/$million value added in the specified assessment period

- 60% of the allocative baseline for activities that have an emissions intensity between 1000 t CO2-e/$million revenue and 1999 t CO2-e/$million revenue or between 3000 t CO2-e/$million value added and 5999 t CO2-e/$million value added in the specified assessment period.

4.13 The Regulations will reduce the rates of assistance (90 or 60%) accorded each emissions-intensive trade-exposed activity at a pre-announced rate, the carbon productivity contribution, of 1.3% a year, to broadly ensure that emissions-intensive trade-exposed activities share in the national improvement of carbon productivity.

4.14 The allocative baselines for each activity will be set in the Regulations taking into account historic emissions and production information submitted to the Department of Climate Change in early 2009. Baselines for allocations will not be updated over time for changes in the emissions intensity of entities conducting emissions-intensive trade-exposed activities in order to maximise abatement incentives, and will be used to determine allocations to new and existing entities conducting a given activity.

4.15 Allocations of assistance to entities conducting emissions-intensive trade-exposed activities will be directly linked to the level of production of individual entities conducting an activity. The previous financial year's production of the activity by the entity will be used to determine a given year's allocations, with the following exceptions:

- in the first year of the Scheme, the average production of the highest two of the last three years will be used
- with regard to new entrants and significant expansions, the Authority will be afforded the discretion to determine the first few years' allocations, to allow for a 'ramp up' period before capacity production levels are achieved.

4.16 If an entity ceases operating an emissions-intensive trade-exposed activity, it will be required to relinquish units that had been allocated to it for production that did not occur.

4.17 Where an emissions-intensive trade-exposed activity is carried out at a single facility, the entity which has, or would have, liability under the Scheme for direct emissions from the facility may apply for assistance. Where more than one entity has liability or potential liability under the Scheme (such as where more than one facility is involved), there must be a joint application from those entities, and that joint application must specify how they want the assistance allocated.

4.18 The emissions-intensive trade-exposed industry assistance program will be reviewed by an expert advisory committee at each five-year review point under Part 25 of the draft bill, or at another date at the request of the Minister. The review of the emissions-intensive trade-exposed assistance program will be in regard to:

- the review of eligibility for activities currently determined to be ineligible for assistance in light of commodity price movements and changes to scheme coverage
- whether modifications should be made to the emissions-intensive trade-exposed assistance program
- whether broadly comparable carbon constraints are applying internationally, at either an industry or economy-wide level, or an international agreement involving Australia and all major emitting economies is concluded, in which case the committee would make recommendations to Government with regard to the withdrawal of emission-intensive trade-exposed assistance.

4.19 The Government also announced in the White Paper a process for affected firms to request the Government to commission further advice from the Productivity Commission pertaining to how the Scheme may be impacting their industry. Such advice would be sought through the provisions of the *Productivity Commission Act 1998*.

4.20 The Government has committed to providing five years' notice of any modifications to the emissions-intensive trade-exposed assistance program, unless the modifications were required for compliance with Australia's international trade obligations.

Summary of Part 8

4.21 A simplified outline of Part 8 is included in the bill ***[Part 8, Division 1, clause 166].***

Introduction

4.22 Division 1 sets out the objects of the Part and consequently the emissions-intensive trade-exposed assistance program. As set out in the White Paper, this is centred around reducing the risk of carbon leakage and providing transitional assistance to emissions-intensive trade-exposed activities.

Formulation of the program

4.23 Division 2 sets out the core components of the emissions-intensive trade-exposed activities program. In particular it provides for:

- the creation of a program in regulations which involves the issuance of free Australian emissions units in respect of activities which are taken to be emissions-intensive trade-exposed activities and are carried on in Australia during a particular financial year
- the program to require the persons issued units under the program to relinquish units in specified circumstances. This is intended to be used to provide for relinquishment of units on the closure of a facility
- the imposition of reporting and record-keeping requirements for persons issued free units under the program. This is intended to be used to ensure the Authority is aware of potential closures and whether production levels claimed in assistance applications were actually produced.

- the program to set out comprehensive application and assessment requirements.

Compliance

4.24 Division 3 requires that persons comply with reporting and record-keeping requirements under the program. Failure to comply will incur a civil penalty.

Other aspects of the program outside of Part 8

4.25 Part 15 Division 2 sets up the legal architecture around compliance with the relinquishment requirements which will operate on the closure of a facility. Accordingly, if a person does not relinquish units as necessary they will be required to pay a penalty, in respect of any units not relinquished, of 200% of the benchmark average auction price of the previous financial year or another amount specified in regulations. If this is not paid, a penalty of 20% per annum is payable or another lower rate specified in regulations.

4.26 There are also provisions requiring the Authority to disclose information about the program in Part 12 of the draft bill. The general enforcement and accountability framework for the Authority is also relevant to the program.

Detailed explanation of provisions

Division 1 - Introduction

Objects

4.27 The object of the Part is set out in the draft bill ***[Part 8, Division 1, clause 165]***

4.28 The objects provision outlines the activity focus of the assistance as the Part is intended to allow the delivery of assistance in respect of emissions-intensive trade-exposed activities ***[Part 8, Division 1, clause 165(a)]***. Accordingly, it is the carrying out of defined activities which creates eligibility for assistance rather than a firm's historic or future emissions.

4.29 Assistance is provided to reduce the risks of ‘carbon leakage’, understood in terms of the incentives on businesses to move production to foreign countries or locate new investment in a foreign country rather than Australia ***[Part 8, Division 1, clause 165(b)].*** Such incentives may be created by

the treatment of emissions and level of regulation to reduce emissions in foreign countries.

4.30 Assistance is also to provide transitional support to such activities when they are carried out in Australia ***[Part 8, Division 1, clause 165(c)]***. This is done through the administrative allocation of Australian emissions units under the program.

4.31 The objects provision recognises that circumstances may change such that assistance may no longer be warranted. In particular, it outlines two distinct circumstances where this may be the case:

- whether sufficient measures to reduce emissions of carbon dioxide and other greenhouse gases have been implemented in respect of the markets in which persons who carry on emissions-intensive trade-exposed activities in Australia compete ***[Part 8, Division 1, clause 165(d)]***

or

- where foreign countries responsible for a substantial majority of the world's emissions have implemented sufficient measures to reduce those emissions ***[Part 8, Division 1, clause 165(e)]*** .

4.32 The Government will determine whether the assistance is no longer warranted based on advice from the expert advisory committee review on the efficacy and appropriate level of coverage of such measures. It should be noted that measures to reduce emissions do not necessarily need to consist of a cap on emissions and other approaches to reduce emissions are also intended to be considered in the analysis. Industry-wide emissions could also be controlled through international sectoral agreements outside the direct control of Governments.

4.33 It is acknowledged that other factors may also come into play which render the assistance unwarranted in terms of its primary objective of addressing carbon leakage and providing transitional assistance ***[Part 8, Division 1, clause 165(f)]***. However, the Government's intention is that the factors listed in the legislation are the primary circumstances where assistance may no longer be warranted.

Division 2 - Formulation of the emissions-intensive trade-exposed assistance program

4.34 This Division allows for the creation of the program in Regulations. The technical aspects of precisely defining emissions-intensive trade-exposed activities and relevant production units, and the

need for flexibility to include new activities, make the program appropriate to locate within regulations rather than the bill itself.

Creating the emissions-intensive trade-exposed assistance program

4.35 The central feature of the Part is the ability for the Regulations to create a program which allocates free Australian emissions units in respect of emissions-intensive trade-exposed activities as defined by the program ***[Part 8, Division 2, clause 167(1)]***. Such activities must be carried on in Australia during an eligible financial year. Assistance may be delivered before an activity is carried on so long as the activity does actually get carried out in the relevant eligible financial year.

4.36 Eligibility requirements for the assistance will be specified in the program which must state that a registry account is one prerequisite. Without a registry account, it would be impossible to allocate the units. It is intended that eligibility will essentially rest upon whether a defined emissions-intensive trade-exposed activity is being carried out, whether relevant levels of production have been achieved and that the person applying is the one ordinarily liable for the emissions from the relevant activity under the scheme ***[Part 8, Division 2, clause 167(2)]***.

4.37 The Minister must take all reasonable steps to establish the program before 1 July 2010 ***[Part 8, Division 2, clause 167(3)]***.

Relinquishment requirement

4.38 The program may provide for the relinquishment of units ***[Part 8, Division 2, clause 168]***. This is intended to be utilised in respect of the closure of an activity. Accordingly, where units are allocated early in a financial year attributable to production that is to take place in that year, and production ceases during the year (other than for maintenance or similar temporary closures), units attributable to the production which did not take place will be required to be relinquished. As a result, such a requirement may be defined in relation to events, circumstances or a decision of the Authority according to criteria in the program ***[Part 8, Division 2, clause 168(1)(b)]***. This provision will ensure that the assistance is contingent upon continued production by the activity and will avoid the potential for an entity to receive a windfall gain from the allocation of units in respect of production which is then closed or moved offshore.

4.39 Relinquishment requirements only apply to persons issued units under the program ***[Part 8, Division 2, clause 168(1)(a)]*** and cannot exceed the number of units issued to the person under the program ***[Part 8, Division 2, clause 168(2)]***.

4.40 The relinquishment of units to comply with the program can be done by submitting an electronic notice to the Authority ***[Part 15, Division 2 clause 286]***.

Reporting requirements

4.41 The program can impose reporting requirements on those persons issued units in accordance with the program. Such requirements will allow the Authority to adequately monitor situations where a closure may have occurred and be alerted to situations where it may need to trigger a relinquishment requirement ***[Part 8, Division 2, clause 169]***.

4.42 Compliance with a reporting requirement is mandatory ***[Part 8, Division 3, clause 173(1)]*** .

Record-keeping requirements

4.43 The program can impose record-keeping requirements on those persons issued units in accordance with the program ***[Part 8, Division 2, clause 170]***. Such requirements will facilitate monitoring of the closure of an activity and ensure that the production records which determined assistance levels are kept for subsequent validation or investigation. As production levels will be the central factor which determines the levels of assistance and these levels will not be collected and reported under the *National Greenhouse and Energy Reporting Act 2007*, this additional provision is necessary. The provisions of Part 18 of the draft bill would also not be applicable because the program is contained within the Regulations rather than the bill itself. However, it is not intended that the provision be used to duplicate other reporting mechanisms or significantly increase the regulatory burden on business.

4.44 Compliance with a record-keeping requirement is mandatory ***[Part 8, Division 3, clause 173(2)]***.

Other matters and ancillary or incidental provisions

4.45 Further details of the program will be specified in the Regulations ***[Part 8, Division 2, clause 171]*** and ***[Part 8, Division 3, clause 172]***. In particular, the Regulations can contain extensive provisions regarding the applications for assistance. Given the value of the units to be allocated, it will be important for the Authority to have sufficient verified information to support the relevant production levels which determine the level of assistance to be allocated in a particular year ***[Part 8, Division 2, clauses 171(1) and 171(2)]***.

4.46 These requirements may include that the information be verified by statutory declaration by a relevant company officer or accompanied by

particular documents such as an assurance report as to whether the production was actually undertaken in the previous financial year or engineering reports to demonstrate that a particular activity is in fact conducted. It is intended that the Authority will establish a single online portal for these applications.

4.47 The provisions allow the regulations to prescribe in full the process and procedural requirements for the Authority to deal with applications. It is anticipated that applications will be made between 1 July and 31 October each year and assessed by the Authority on a case by case basis. The Authority will be able to issue units to applicants as soon as it is sufficiently satisfied in relation to each application.

4.48 The program can also include ancillary or incidental provisions ***[Part 8, Division 2, clause 172]***.

4.49 It is also intended that the emissions-intensive trade-exposed assistance program will, where necessary, adopt various industry standards and confer administrative decision making functions on the Authority ***[Part 26, clause 384]*** and ***[Part 26 , clause 385]***.

Division 3 - Compliance with reporting and record-keeping requirements under the emissions-intensive trade-exposed assistance program

Compliance with record-keeping and reporting requirements

4.50 There is a direct obligation to comply with any record-keeping or reporting requirements. Those persons with a direct obligation to comply with reporting and record-keeping requirements and others involved in a breach or potential breach of reporting or record-keeping requirements are liable for their behaviour ***[Part 8, Division 3, clause 173]***.

4.51 Breaches of these requirements are all civil penalty provisions and can accordingly be enforced under Part 21 of the draft bill discussed in Chapter 9 below ***[Part 8, Division 3, clause 173(4)]***.

Part 15, Division 3 - Compliance with relinquishment requirements

4.52 A financial penalty will be imposed when units are not relinquished as required under the program ***[Part 15, Division 3, clause 287]***. Division 3 of Part 15 of the draft bill contains a number of provisions relating to the calculation of the financial penalty, late payment of penalties, recovery of penalties, set offs and refunds of overpayments. These are similar to the provisions of Division 4 of Part 6 and are explained in Chapters 8 and 9 below.

Public disclosures relating to emissions-intensive trade-exposed assistance program

4.53 The public will be informed about units issued under the program ***[Part 12, Division 4, clause 273]*** and ***[Part 12, Division 4, clause 274]***. This will inform the market as to how many units are available for auctioning and will provide public accountability for the application of the emissions-intensive trade-exposed assistance program. In particular, the Authority is required to publish on its website a notice when Australian emissions units are allocated to a person under the program which includes the number of units issued to that person and the activity for which they were issued ***[Part 12, Division 4, clause 273(1)]*** .

4.54 The total number of Australian emissions units issued during a particular quarter must be published on the Authority's website. This information must also be published in respect of each activity ***[Part 12, Division 4, clause 274]***.

4.55 The total number of Australian emissions units claimed under the program but for which no decision has been made must also be disclosed. This will give the market an idea about the potential number of units which may not be available for auctioning ***[Part 12, Division 4, clause 274(c)]***.

Administration, enforcement and monitoring of the program

4.56 The program will be administered by the Australian Climate Change Regulatory Authority referred to as the Authority for the purposes of the draft bill. It will be subject to the governance arrangements in its establishment Act and this bill. These include secrecy provisions to protect confidential information submitted in relation to the program (See Australian Climate Change Regulatory Authority Bill 2009, Part 3, clause 43).

4.57 The Authority's decisions on eligibility and delivery of Australian emissions units under the program will be subject to the review procedure outlined in Part 24 of this draft bill. This includes merits review in the Administrative Appeals Tribunal.

4.58 The Authority will be able to draw upon its enforcement powers in Parts 17 to 23 of this draft bill to enforce the requirements of the program. The intention is to provide clear application requirements so that the Authority has clear, audited and comprehensive information upfront to make decisions upon allocations. This should allow a light-handed risk-based approach to monitoring and enforcement issues associated with the program.

4.59 Should there be concerns about production levels relevant to allocations or whether a closure requirement can be triggered, it is envisaged that the Authority would be able to require an external auditor to be appointed and report back on what has taken place. This would be similar to section 73 of the *National Greenhouse and Energy Reporting Act 2007*.

Chapter 5
Coal-fired electricity generation

Outline of chapter

5.1 This chapter outlines the effect of the provisions of Part 9 of the draft Carbon Pollution Reduction Scheme Bill 2009, which implement the Government's Electricity Sector Adjustment Scheme. Part 9, Division 2 and Part 9, Division 3 set out the provisions by which the Authority will determine the number of free Australian emissions units to issue to eligible coal-fired electricity generators under the Electricity Sector Adjustment Scheme.

5.2 Part 9, Division 4 provides that a portion of the Australian emissions units available to be issued to an eligible coal-fired electricity generators can be withheld in the event that this asset may be likely to receive a 'windfall gain' under the Electricity Sector Adjustment Scheme, that is, where the value of assistance a generator receives exceeds the likely loss in asset value it faces under the Carbon Pollution Reduction Scheme (the Scheme).

5.3 Part 9, Division 5 requires that no Australian emissions units be issued to generators that do not comply with the power system reliability test, to decrease the already low likelihood that the Scheme will reduce the reliability of supply in Australia's electricity markets.

Context and object of Part 9

5.4 The introduction of the Scheme will impose a new cost on fossil fuel-fired electricity generators. The general level of electricity prices will rise as generators include this cost into their offers to supply electricity to customers.

5.5 However, relatively emissions-intensive generators are likely to face a greater increase in their operating costs than the general increase in the level of electricity prices. Competition from relatively less emissions-intensive generators, which face lower costs under the Scheme, may cause these emissions-intensive generators to lose profitability.

5.6 The generation of electricity is a capital-intensive process. Investors in this sector purchase or construct complex and expensive

machinery that can generate large amounts of electricity in a cost-effective way. To finance the purchase or construction of a generator, investors will generally borrow money from creditors. Ongoing investment in the electricity generation sector requires investors to deploy capital based on their assessment of the risk and return of that investment, with creditors supplementing this capital with debt finance. Ongoing investment in this sector is important to maintain or improve the performance of existing assets and to deliver new, lower-emissions generation technologies.

5.7 The risk premium charged by investors and creditors to make an investment reflects their perceptions of its risk in comparison to alternate investments. The Scheme will change the relative risk and return of particular investments based on the amount of greenhouse gas emissions they produce. However, if investors consider that the regulatory environment is riskier as a result of the Government having introduced the Scheme, all investments in the sector could face an increased risk premium irrespective of the amount of greenhouse gas emissions they produce, which in turn could affect their cost or timing.

5.8 The Government considers that investors' perceptions of the risk of investing in the Australian electricity generation sector are most likely to be affected by the extent of extreme losses in this sector that may arise under the Scheme, rather than by the average level of loss. Targeted allocations of free Australian emissions units to the most affected generators can partially offset these losses of asset value and thereby reduce the impact of the Scheme on investor confidence.

5.9 Investors who purchase or construct generation assets after the Commonwealth Government's announcement of its support for a scheme to reduce pollution caused by emissions of carbon dioxide and other greenhouse gases are able to factor the impact of such a scheme on their investments. Providing assistance to these investors would not address a loss of asset value resulting from Government policy, but would instead address a loss of asset value resulting from an incomplete risk assessment by the investor.

5.10 By contrast, investors who purchased or constructed generation assets prior to the Commonwealth Government's announcement of its support for such a scheme may face losses of asset value as a result of the introduction of a carbon constraint. Whilst such a policy change could have been foreseen prior to this announcement, the Government considers it appropriate to partially recognise losses of asset value experienced by investors that were committed to such investments prior to a clear announcement by the Commonwealth Government of its support for such a scheme.

5.11 On 3 June 2007, the then Prime Minister announced that "Australia will move towards a domestic emissions trading scheme, that's a cap and trade system beginning no later than 2012". The Electricity Sector Adjustment Scheme limits eligibility for assistance to those generation assets that were in operation, or committed to be constructed, by 3 June 2007.

5.12 This context is summarised in the object of Part 9, which focuses on the maintenance of investor confidence in electricity generation ***[Part 9, Division 1, clause 174]***. Nonetheless, the Government recognises the importance of the proper regulation of electricity markets for continued efficient investment in electricity generation. The Government is confident that the Electricity Sector Adjustment Scheme embodied in Part 9 of the draft bill will complement the continued reform of energy market regulatory frameworks in promoting efficient investment and reliable supply in Australia's electricity markets.

Summary

5.13 Part 9, Division 1 sets out an objects clause ***Part 9, Division 1, clause 174]*** and a simplified outline for the Part ***[Part 9, Division 1, clause 175]***.

5.14 Part 9, Division 2 requires the Authority to issue a number of free Australian emissions units in respect of particular generation assets based on the annual assistance factors specified in various certificates of eligibility for coal-fired generation assistance in force in respect of those assets, and clarifies the persons to whom the Authority should provide these free Australian emissions units.

5.15 Part 9, Division 3 sets out the circumstances under which the Authority should issue a certificate of eligibility for coal-fired generation assistance, and determines how the Authority should determine an annual assistance factor in each of those certificates.

5.16 Part 9, Division 4 provides that the issuing of some free Australian emissions units available under this Part is subject to the Minister's power to make a determination withholding those units, in the event that the Authority finds that the provision of assistance under this Part is likely to deliver a 'windfall gain' in respect of a particular generation asset.

5.17 Part 9, Division 5 provides that generation assets in respect of which certificates of eligibility for coal-fired generation assistance are issued must comply with the power system reliability test in order to be issued with free Australian emissions units under this Part.

Detailed explanation of new law

Important definitions used in this Part

5.18 Part 9 is based upon some key concepts defined in the draft bill. Assistance under Part 9 is not provided in respect of a particular person, such as the person making an application for assistance, but rather is provided in respect of a collection of equipment used for the generation of electricity known as a 'generation asset'. Understanding the definition of a generation asset ***[Part 1, clause 5, definition of 'generation asset']***, and the subsidiary concepts of 'generation unit' ***[Part 1, clause 5, definition of 'generation unit']***, 'generation complex' ***[Part 1, clause 5, definition of 'generation complex']*** and 'generation complex project' ***[Part 1, clause 5, definition of 'generation complex project']***, is essential to understanding the scope of the operation of Part 9.

5.19 The concept of a generation asset ***[Part 1, clause 5, definition of 'generation asset']*** is not the same as the concept of a 'facility', which takes its definition from the *National Greenhouse and Energy Reporting Act 2007*. Assistance under Part 9 is focused on coal-fired electricity generators, which must meet certain eligibility criteria. However, a facility under the *National Greenhouse and Energy Reporting Act 2007* could include, for example, the activities of a co-located coal-fired generator and coal mine. For this reason, the separate definition of a 'generation asset' is used to capture those elements of a facility that may be eligible for coal-fired generation assistance.

5.20 For operational reasons, equipment used for the generation of electricity is often engineered such that at, a given location, there are multiple sets of equipment that can generate electricity independently of one another (although they may share some common infrastructure, such as cooling systems or coal conveyor belts). Under the draft bill, each independent set of equipment for the generation of equipment is known as a 'generation unit' ***{Part 1, clause 5, definition of 'generation unit']***, whilst one or more generation units at the same location are known as a 'generation complex' ***[Part 1, clause 5, definition of 'generation complex']***. Assistance under this Part is provided in respect of generation complexes rather than generation units. There is no requirement on persons applying for assistance under Part 9 to aggregate multiple generation units at the same location together to form a single generation complex, although this may be practical for various reasons. However, a person applying for assistance under Part 9 should factor into its decision the aggregate of multiple generation units to form a single generation complex, the fact that each generation unit in the generation complex must satisfy the eligibility criteria in order for the generation complex to pass the generation asset assistance eligibility test ***[Part 9, Division 3, clause 181]***.

5.21 Further, assistance under Part 9 is available to projects to construct and commission a new generation complex that were fully committed by their proponent as of 3 June 2007 (see 5.33 below). Accordingly, the draft bill provides the concept of a 'generation complex project' ***[Part 1, clause 5, definition of 'generation complex project']***, which is a project to construct and commission a new generation complex. The definition of a generation asset includes both generation complexes and generation complex projects.

Applying for assistance

5.22 A person who wishes to be issued with free Australian emissions units under this Part must apply to the Authority to receive a certificate of eligibility for coal-fired generation assistance ***[Part 9, Division 2, clause 177]***. Applications must be made within 90 days of the commencement of the provision ***[Part 9, Division 2, sub-clause 177(1)]***. Applications are made in respect of a generation asset, rather than in respect of the person making the application ***[Part 9, Division 2, sub-clause 177(1)]***. Similarly, the recipient of assistance is defined in respect of a generation asset, not in respect of the person who applied for assistance ***[Part 9, Division 2, sub-clause 176(6)]***.

5.23 Spurious applications from persons that do not own, operate or control the generation asset in respect of which the application is made are prevented ***[Part 9, Division 3, sub-clause 177(2) and 177(3)]***. The concept of 'owning, controlling or operating' a generation asset is intended to have the same meaning as the equivalent terms in laws relating to the regulation of energy markets that require the registration of electricity generators. The primary laws (and subordinate instruments) relating to the regulation of energy markets that are likely to be relevant to the application of this Part are:

- in relation to the National Electricity Market, the National Electricity Rules as made and amended under Part 7 of the Schedule to the *National Electricity (South Australia) Act 1996* of South Australia and given force of law in other jurisdictions through application legislation

- in relation to the Western Australian Wholesale Electricity Market, the Wholesale Electricity Market Rules provided for under section 123 of the *Electricity Industry Act 2004* of Western Australia and the *Electricity Industry (Wholesale Electricity Market) Regulations 2004*.

5.24 Multiple applications cannot be made in respect of all or part of a generation asset ***[Part 9, Division 3, sub-clause 177(4) and 177(5)]***. The recognition and consideration of overlapping applications by the

Authority could result in an excessive issuance of certificates of eligibility for coal-fired generation assistance and of annual assistance factors, and thereby deliver additional, unwarranted assistance in respect of some generation assets.

5.25 There are a number of requirements on an application for the issuance of free Australian emissions units ***[Part 9, Division 2, clause 178]***. In particular, applications in respect of a generation asset that entered service after 1 July 2004 are required to provide an independent engineering report ***[Part 9, Division 3, clause 178(1)(e) and 178(3)]***. This information is required to assist in the Authority's assessment of the emissions intensity of such an asset under ***[Part 9, Division 3, clause 182(4)]***.

5.26 Regulations may require particular documents to be provided with an application for coal-fired generation assistance ***[Part 9, Division 3, clause 178(1)(d)]***. The Government intends to make regulations requiring these documents to include a statement provided by an appropriate audit firm to the effect that the data and information provided as part of this application has been assessed to be free of material misstatement. Information may also need to be verified by statutory declaration ***[Part 9, Division 3, clause 178(2)]***.

5.27 Having received an application, the Authority may consider that it requires additional information to properly assess it. The Authority is able to require further information to assist its assessment ***[Part 9, Division 3, clause 179]***. This may be an iterative process where the Authority requests information more than once to clarify the issues involved. The Authority is provided additional time to make its decision on an application where additional information is required ***[Part 9, Division 3, sub-clause 180(4)(b)]***.

The Authority's assessment

5.28 Ordinarily, the Authority will use its best endeavours to make an assessment within a 90 day period from the date of the application ***[Part 9, Division 3, clause 180(4)(b)]***. To ensure that the Authority has sufficient information to make a decision, it is provided with an additional 90 days to make its decision on an application where additional information has been requested ***[Part 9, Division 3, clause 180(4)(a)]***. Where more than one request for information is made, this would apply to the latest of those requests. However, nothing prevents the Authority from making a decision before the end of the standard or extended period where it is able to do so.

5.29 The Authority's assessment of an application involves two key elements:

- determining the eligibility of the generation asset in respect of which the application is made
- determining an annual assistance factor in respect of that generation asset.

The annual assistance factor is crucial to determining the total number of free Australian emissions units that will be issued in respect of that generation asset in accordance with this Part.

Determining eligibility

5.30 The Authority must apply the generation asset assistance eligibility test to decide whether to issue a certificate of eligibility for coal-fired generation assistance ***[Part 9, Division 3, clause 181(1) and 180(2)]***. In order to issue such a certificate, the Authority must be satisfied that a generation asset passes this test in one of two ways:

- a generation complex must pass the test ***[Part 9, Division 3, clause 181(2)]***
- a generation complex project must pass the test ***[Part 9, Division 3, clause 181(3)]***.

5.31 Assistance for coal-fired electricity generators under this Part is provided to address significant declines in the asset values of generation assets that were invested in before the Commonwealth Government announcement of support for a scheme to reduce pollution caused by emissions of carbon dioxide and other greenhouse gases ***[Part 9, Division 1, clause 174].*** As explained in 5.11 above, this point in time was 3 June 2007.

5.32 Therefore, the generation asset assistance eligibility test seeks to determine whether a generation complex was 'in operation' in June 2007, or whether a generation complex project was 'committed' to be constructed as of 3 June 2007. The use of the month of June 2007 for generation complexes, in contrast to the date of 3 June 2007 for generation complex projects, simply reflects the practicality of determining whether a generation unit was in operation at any time during that month, given that generation units that are 'in operation' may be offline for a period of time for various operational reasons.

5.33 Generation complex projects may receive assistance if, as of 3 June 2007, they were sufficiently committed that the project could not have been substantially altered in response to the new information about the Commonwealth Government's climate change policies that emerged at that time. The Government considers that the definition of a 'committed project' from Rule 11.10A.1 of the National Electricity Rules, which sets

out criteria as to whether a generation project should be considered to be fully committed by its proponent, is appropriate to replicate here for a similar purpose ***[Part 9, Division 3, clause 181(3)(b)]***.

5.34 Some generation assets are capable of reducing emissions at relatively low cost by substituting coal in their generation process with an alternative lower-emissions fuel, such as natural gas. Accordingly, the Government decided that these assets would not be eligible for assistance. To pass the generation asset eligibility test, generation complexes must use coal as their primary energy supply, as indicated by 95% of the electricity it generated in financial year 2006-07 having been attributable to the combustion of coal ***[Part 9, Division 3, clause 181(2)(b)]***.

5.35 The Government has also determined that generation assets must be connected to an electricity grid of a sufficient size that the asset could be considered to be exposed to significant competition in order to warrant assistance under the Electricity Sector Adjustment Scheme. Accordingly, generation assets must be connected to a grid with a capacity of at least 100 megawatts in order to pass the generation asset assistance eligibility test ***[Part 9, Division 3, clause 181(2)(c)]***. The capacity of the grid used in the draft bill is the same as the threshold size of an electricity grid used in the *Renewable Energy (Electricity) Act 2000* to determine those sales of electricity that will be liable to the provisions of that Act. The method for calculating the capacity of a grid used in the draft bill is also the same as under the *Renewable Energy (Electricity) Act 2000* and regulations made under that Act, in that it excludes standby and privately-owned domestic generation sources ***[Part 9, Division 3, clause 181(4)]***.

5.36 In relation to generation complex projects, the Authority must make assessments of whether a generation asset uses coal as its primary energy supply, and whether it is connected to an electricity grid of a sufficient size that it is exposed to significant competition, against what was proposed for the project as of 3 June 2007 ***[Part 9, Division 3, clauses 181(3)(c) and 181(3)(d)]***.

5.37 If the Authority refuses to issue a certificate of eligibility for coal-fired generation assistance, the Authority must notify the applicant of this decision ***[Part 9, Division 3, clause 180(5)].***

Determining the annual assistance factor

5.38 A certificate of eligibility for coal-fired generation assistance must include an annual assistance factor ***[Part 9, Division 3, clause 180(3)]***. This factor is used to determine the correct number of Australian emissions units to issue in respect of a particular generation asset ***[Part 9, Division 2, clause 176(2)]***. The annual assistance factor can be zero, in which case no Australian emissions units would be issued in respect of that

generation asset, even though it passed the generation asset assistance eligibility test.

5.39 The determination of an appropriate annual assistance factor involves some estimation and uncertainty. Therefore, ***[Part 9, Division 3, clause 182(1)]*** makes clear that the annual assistance factor is the Authority's reasonable estimate of the number calculated in accordance with this clause, rather than a precise calculation of such a number.

5.40 The two key elements used in the formula to determine the annual assistance factor for a generation asset are:

- its historical energy
- its emissions intensity.

[Part 9, Division 3, clause 182]

These elements are combined such that the annual assistance factor for a generation asset is the product of its historical energy and the difference between its emissions intensity in kilotonnes of carbon dioxide equivalence of emissions per gigawatt hour of electricity and a 'threshold' level of emissions intensity of 0.86 kilotonnes of CO_2-e per gigawatt hour of electricity generated. The manner in which the figure of 0.86 kilotonnes of CO_2-e per gigawatt hour of electricity generated was reached was described at pages 13-24 to 13-26 of the White Paper.

Historical energy

5.41 Ideally, the measure of historical energy used for a generation asset would be its actual output over the three year period from 1 July 2004 to 30 June 2007. This measure is used for generation complexes that entered service on or before 1 July 2004 ***[Part 9, Division 3, clause 182(1)(a)]***. However, using this measure for generation assets that entered service after 1 July 2004 would unfairly reduce their annual assistance factor, and consequently the number of free Australian emissions units they receive. Therefore, for generation complexes or generation complex projects that entered service after 1 July 2004, the 'nameplate rating' of the generation asset is used to calculate a proxy for its likely energy output over a notional three year period ***[Part 9, Division 3, clause 182(1)(b)]*** and ***[Part 9, Division 3, clause 182(1)(c)]***.

5.42 The nameplate rating of a generation asset is its maximum continuous electrical generation capacity as registered with the appropriate energy market operator ***[Part 1, clause 5, definition of 'nameplate rating']***. Accordingly, the output of the asset can be estimated by considering the likely 'capacity factor' of the asset, that is, the percentage

of its maximum output that an asset produces on average over a period of time. Multiplying the nameplate rating of the generation asset in megawatts by 21.024 approximates the energy output (in gigawatt hours) of such a generator over a notional three year period if it operates at an 80%'capacity factor' over that period, that is, if its average output over the period is 80% of its maximum output. The number 21.024 has been worked out by firstly calculating the number of hours in a three year period, which is the number of days in a year, 365, multiplied by the number of hours in a day, 24, multiplied by the number of years in the period, three. This number is then multiplied by 0.8 to reflect the assumed 80% capacity factor of the generation asset. Lastly, this number is divided by 1000 to convert a number that would approximate the generation asset's output in megawatt hours to an approximate output in gigawatt hours, as required by the formula.

Emissions intensity

5.43 Broadly, the emissions intensity of a generation asset is the emissions produced by the asset divided by the amount of electricity it generates. These two elements of emissions intensity could be either estimated from the historical performance of an asset or from its likely future performance. Therefore, as for historical energy, the draft bill uses different methods to estimate a generation asset's emissions intensity depending on whether or not it had entered service on or before 1 July 2004.

5.44 For a generation asset that entered service on or before 1 July 2004, the emissions intensity is estimated by reference to the actual emissions and actual energy output of the asset over the three year period from 1 July 2004 to 30 June 2007 ***[Part 9, Division 3, clause 182(2)].*** Importantly, these emissions must be 'emitted from the combustion of fuel in the generation complex' and therefore would not include, for example, the combustion of fuel to operate mining equipment. Further, the combustion of fuel must be for 'the purposes of the generation of electricity' and therefore would not include, for example, emissions created for the purposes of the production of steam in a cogeneration plant. The energy output of the generation asset, described as the 'gigawatt hours of electricity generated', is exactly the same number as in ***[Part 9, Division 3, clause 182(1)(a)].***

5.45 For a generation asset (whether a generation complex or a generation complex project) that entered service after 1 July 2004, the Authority has a broad discretion to estimate its emissions intensity ***[Part 9, Division 3, sub-clause 182(4)]***. For example, the Authority might use design documents to estimate the thermal efficiency of the generation asset, that is, how efficiently it turns a quantity of fuel into electricity, and fuel contracts to estimate the emissions released from the combustion of a

given quantity of the fuel used or intended to be used in the generation asset. These two elements could allow the Authority to estimate the theoretical emissions intensity of a generation asset, whether or not it has yet entered service. These estimates should be supported by the independent engineering report that is required to be provided with an application in respect of a generation asset that entered service after 1 July 2004 ***[Part 9, Division 3, clause 178(1)(e)]***.

5.46 The Authority may have regard to an estimate of the emissions intensity of the generation asset based on its actual performance during the period it has been in service, but the Authority is not required to adopt this estimate as the emissions intensity of the asset ***[Part 9, Division 3, clause 182(4)(c) and 182(5)].*** If the period the asset has been in service is short, estimates of emissions intensity based on this period may be misleading due to the small sample size of measurements of, for example, coal quality. Further, the initial period of operation of a new generation asset can involve activities that might cause estimates of the asset's emissions intensity over this period to be unrepresentative of its likely general level of performance. For example, a generation asset's early period of operation might involve testing the asset's ability to operate at output levels above or below its most efficient level of operation, or starting and stopping the asset an unusually high number of times. These uncertainties support the high level of discretion afforded the Authority in estimating emissions intensity in this circumstance. The Authority will weigh up the strength and veracity of the information presented in the application and its own analysis in making its decision.

5.47 The definition of emissions intensity used for generation assets that entered service after 1 July 2004 differs from that used for generation assets that entered service on or before 1 July 2004 in being non-specific in the period of time over which the estimate is made ***[Part 9, Division 3, clause 182(5)]***. For example, if a generation asset entered service on 1 July 2005, the Authority may be able to estimate the emissions intensity of the asset over a period of operation spanning from 1 July 2005 to around 30 June 2009. However, for a generation asset that did not enter service until 1 July 2008, the Authority may only have a period from 1 July 2008 to around 30 June 2009 from which to consider performance data.

5.48 Where the Authority's estimate of emissions intensity is less than 0.86, the emissions intensity used in the annual assistance factor formula is taken to be 0.86 ***[Part 9, Division 3, clause 182(3) and 182(6)]***. This means that the annual assistance factor for such a generation asset will be zero and, in turn, that no free Australian emissions units will be issued to such an asset under ***[Part 9, Division 2, clause 176(2)].*** These provisions also prevent the calculation of an annual assistance factor that is below zero,

which would distort the allocation methodology applied under ***[Part 9, Division 2, clause 176(2)].***

How annual assistance factors will be calculated

Example 5.1 A generation asset that entered service on or before 1 July 2004

To estimate the historical energy of a generation asset that entered service on or before 1 July 2004, the applicant should provide, and the Authority should assess, historical data relating to the generation of electricity by that generation asset over the period from 1 July 2004 to 30 June 2007. The Authority could verify this data through comparison with data publicly available from independent bodies such as the market operator in the market in which the generation asset operates. For example, this investigation might find that the historical energy of the generation asset over the three year period in question was 22 950 gigawatt hours.

To estimate the emissions intensity of a generation asset that entered service on or before 1 July 2004, the applicant should provide, and the Authority should assess, historical information relating to the coal usage and coal quality of the generation asset over the period from 1 July 2004 to 30 June 2007. For example, this investigation might find that the generation asset used approximately 28 500 000 tonnes of coal, with an average energy content of 11 gigajoules per tonne. Historical analyses of coal quality might indicate that the combustion of the coal produced, on average, 0.093 tonnes of CO_2-e per gigajoule of fuel combusted. These estimates indicate that the generation asset produced approximately (28 500 000 × 0.093 × 11) tonnes of CO_2-e, or 29 155.5 kilotonnes of CO_2-e, over the three year period in question.

Based on these estimates, the Authority's reasonable estimate of the generation asset's emissions intensity would be 29 155.5 ÷ 22 950 kilotonnes of CO_2-e per gigawatt hour, or 1.270 kilotonnes of CO_2-e per gigawatt hour.

Accordingly, the Authority would find the generation asset's annual assistance factor to be 22 950 × (1.270 – 0.86), or 9 409.500.

Example 5.2 A generation asset that entered service after 1 July 2004

To estimate the historical energy of a generation asset that entered service after 1 July 2004, the applicant should provide the Authority with the nameplate rating of the generation asset as registered with the relevant market operator. For example, the generation asset's nameplate rating might be 500 megawatts. This being the case, the Authority would estimate the historical energy of the generation asset over a notional three year period to be (500 × 21.024), or 10 512 gigawatts.

To assist the Authority to estimate the emissions intensity of a generation asset that entered service after 1 July 2004, the applicant should provide an independent engineering report setting out an estimate of the emissions intensity of the generation asset. This report might show, and the Authority might verify, facts such as:

- the thermal efficiency of the generation asset, for example, that the generation asset is, on average, capable of converting 11.5 gigajoules of fuel into 1 megawatt hour of electricity

- analyses of the quality of the coal that have been or will be supplied to the generation asset under its established fuel contracts, for example, that the combustion of this coal will produce approximately 0.089 tonnes of CO_2-e per gigajoule of fuel combusted.

The Authority can use estimates to calculate an estimated emissions intensity of the generation asset. For example, the estimates above would indicate that the generation asset in question would release (11.5 × 0.089), or 1.024, tonnes of CO_2-e per megawatt hour of electricity generated. This is also equivalent to 1.024 kilotonnes of CO_2-e per gigawatt hour of electricity generated.

These estimates could also be verified by comparison with the actual performance of the generation asset over its period of operation, if this data is available over a sufficient period of time, to offer reliable additional information to assist the Authority's verification of the independent estimate of emissions intensity.

Based on these estimates, the Authority would find the generation asset's annual assistance factor to be 10 512 × (1.024 – 0.86), or 1 723.968.

Issuing assistance

5.49 The Authority must decide whether or not to issue a certificate of eligibility for coal-fired generation assistance in relation to each individual application it receives and, if so, what the annual assistance factor in the certificate should be ***[Part 9, Division 3, clause 180]***. These decisions will be individually subject to the reconsideration and merits review provisions of Part 24. In other words, the eligibility of, and annual assistance factor calculated in respect of, each individual generator, is determined independently of every other generator, and are individually subject to the review processes in Part 24.

5.50 However, the number of free Australian emissions units that should be issued in respect of a generation asset is a function of not only the annual assistance factor specified in respect of that generation asset,

but also all other annual assistance factors specified in respect of all other generation assets ***[Part 9, Division 2, clause 176(2)]***.

5.51 This is the case because the Authority must take the annual assistance factor in each certificate of eligibility for coal-fired generation assistance and divide it by the sum of all annual assistance factors in all such certificates (the 'total annual assistance factors for that eligible financial year'). This number, which must be less than 1, is then multiplied by the 'generation assistance limit for that eligible financial year' to determine the share of each year's pool of free Australian emissions units that should be issued in respect of that generation asset for that year (subject to the rounding provisions of ***[Part 9, Division 2, clause 176(3)]***). In this way, the available pool of Australian emissions units per year is distributed amongst all eligible recipients of these units in each of the first five years of the Scheme, and the Government's policy of 'capping' the total number of Australian emissions units to be issued under the Electricity Sector Adjustment Scheme is achieved.

Example 5.3 Calculating the number of free Australian emissions units to issue to particular generation assets

Example 1.1 and Example 1.2 outlined the calculation of annual assistance factors for two hypothetical generation assets. These generation assets, which we shall call "Generation asset A" and "Generation asset B", had annual assistance factors of 9 409.500 and 1 723.968 respectively.

Other generation assets are likely to be found to be eligible for assistance, and to be issued certificates of eligibility for coal-fired generation assistance containing annual assistance factors. For example, these annual assistance factors, including those of Generation asset A and Generation asset B, might add up to 69 100.000.

In this case, Generation asset A and Generation asset B would receive the following number of free Australian emissions units in each of the first, second, fourth and fifth years of assistance (provided they comply with the power system reliability test and that the Minister has not made a declaration under in respect of those generation assets):

- Generation asset A = (9 409.500 ÷ 69 100.000) × 26 140 000
  = 3 559 541.3
  = 3 599 500 (after rounding)

- Generation asset B = (1 723.968 ÷ 69 100.000) × 26 140 000
  = 652 161.63
  = 652 200 (after rounding)

In the third year, the number of free Australian emissions units issued to these generation assets would depend on the number of additional

units issued as a result of review events. In the event that no successful reviews of annual assistance factors were concluded prior to 1 September 2012, these generation assets would receive the number of units calculated above in the third year of assistance.

5.52 Ordinarily, a review that changes the annual assistance factor determined in respect of a generation asset would change the 'total annual assistance factors for that eligible financial year' and so would change the number of free Australian emissions units that should have been issued in respect of all other generation assets with a certificate of eligibility for coal-fired generation assistance. This situation would create significant uncertainty for recipients of assistance as it could, for example, involve the relinquishment of incorrectly issued units to the Authority. To prevent this circumstance from requiring alterations to all previous issuances of assistance, the definition of the 'total annual assistance factors for that eligible financial year' includes certificates purportedly issued by the Authority, that is, it includes annual assistance factors in certificates that were found to have been issued incorrectly by the Authority through a review process ***[Part 9, Division 2, clause 176(2)]***. This means that the 'total annual assistance for that eligible financial year' cannot change after 1 September of each financial year and that previous issuances of assistance to a given generation asset will not be altered due to a review of an annual assistance factor determined in respect of a different generation asset.

5.53 However, a review could require the issuance of additional free Australian emissions units in respect of the generation asset that was the subject of the review. In this event, the fact that other allocations are not adjusted could mean that the number of units issued in a given financial year could exceed the Government's cap for that year. The Government has committed to issue 130,700,000 free Australian emissions units over the first five years, or 26,140,000 Australian emissions units in each of five years. The generation assistance limit for the first, second, fourth and fifth years of the Scheme is 26,140,000 ***[Part 9, Division 2, clause 176(2)]***. However, the generation assistance limit is adjusted in the third year of the Scheme to ensure that the number of units issued over the first three years of the Scheme does not exceed 78,420,000 (or three times 26,140,000) when taking into account the 26,140,000 units issued on each of 1 September 2010 and 1 September 2011, and any additional units that may have been issued as a result of a review ***[Part 9, Division 2, clause 176(2) and 176(4)]***. The adjustment also takes into account units withheld as a result of a generation complex failing the power system reliability test ***[Part 9, Division 5, clause 188]***. This adjustment mechanism ensures that the Government's overall cap is not breached as a result of any reviews of annual assistance factors that are resolved prior to 1 September 2012. However, the Government's overall cap could be breached in the unlikely event that a review of a generation asset's annual assistance factor did not

conclude until after 1 September 2012. The adjustment is performed in the third year so that it precedes the windfall gain review, which affects the issuance of free Australian emissions units in the fourth and fifth years of the Scheme.

5.54 The Authority's allocation decisions under ***[Part 9, Division 2, clause 176]*** will not be subject to the review processes in Part 24 as they simply involve the mechanical application of a formula to determine the correct number of free Australian emissions units to issue in respect of a particular generation asset, and the correct application of the provisions that determine the correct recipient of assistance in respect of that generation asset ***[Part 9, Division 2, clause 176(6)]***. Judicial review will remain available if, for example, the incorrect number or units are allocated or units are issued to the wrong recipient.

5.55 The Authority must publish each certificate of eligibility for coal-fired generation assistance as soon as practicable after it is issued ***[Part 9, Division 3, clause 180(6)]***. This is important because, as outlined above, the number of free Australian emissions units issued in respect of a generation asset, is a function of not only the annual assistance factor specified in the certificate of eligibility for coal-fired generation assistance issued in respect of that asset, but also all other annual assistance factors specified in respect of all other generation assets. Accordingly, the public disclosure of the issue of all certificates of eligibility for coal-fired generation assistance, and the annual assistance factors in those certificates, is important to ensure that all potential recipients of assistance have access to information that impacts on the allocation of units under this Part.

5.56 Free Australian emissions units that are issued in respect of a particular generation asset are issued to the entity that was liable for the emissions created from the operation of that asset as of the end of the previous financial year ***[Part 9, Division 2, clause 176(6)].*** To achieve this, it is assumed that the generation asset was a facility, and that this facility emitted sufficient greenhouse gases to meet the Scheme's threshold for liability. The provisions of the draft bill that determine liability for emissions under the Scheme are then applied to identify the recipient of assistance ***[Part 9, Division 2, clause 176(6)]***. In this way, the recipient of assistance identified under this sub-clause is one of three possible persons:

- the controlling corporation of a group where one or more members of the group has operational control of the asset
- the non-group entity with operational control of the asset

or

- the person with a liability transfer certificate in relation to the facility that includes the generation asset (for example, a company with financial control of the facility).

5.57 The issue of units under Part 9 is subject to all of the following:

- the person in receipt of those units must make a submission to the Authority about whether or not the generation asset in question is likely to receive a 'windfall gain' (see below) due to the provision of free Australian emissions units
- the generation asset must not be the subject to a windfall gain declaration and a determination by the Minister following the assessment of whether or not a windfall gain is likely
- the generation asset must comply with the power system reliability test

[Part 9, Division 2, clause 176(9)]

Windfall gain review

5.58 The issuance of free Australian emissions units in respect of any given generation asset is subject to the provisions of Part 9, Division 4. This Division implements the Government's policy that recipients of coal-fired generation assistance must subject themselves to a review to minimise the prospect of them receiving a 'windfall gain' in respect of a generation asset. This review applies individually to each generation asset in respect of which free Australian emissions units are issued under this Part.

5.59 The introduction of a scheme to reduce pollution caused by emissions of carbon dioxide and other greenhouse gases would ordinarily be expected to reduce the value of a generation asset that produces a large amount of greenhouse gases. However, the introduction of such a scheme could provide a generation asset with a 'windfall gain' where, as part of the introduction of the Scheme, the Government provides assistance in respect of that asset and the value of the assistance exceeds the negative impact of the introduction of the Scheme on the value of the asset.

5.60 However, it is impossible to precisely estimate the impact of the introduction of the Scheme on the value of a generation asset. This is particularly the case for projections of the likely impact of the Scheme on a generation asset into the future, but also applies to estimations of the impact of the Scheme on a generation asset made after the event as it can be difficult to know in retrospect what would have occurred had the Scheme never been introduced. These inherent uncertainties in the

windfall gain review are reflected in the design of the review as set out below.

Decision-making structure of the review

5.61 The decision-making structure of the windfall gain review reflects the inherent uncertainty of the assessment at hand. The first step of the process requires the Authority to apply the 'windfall gain test' to each generation asset in respect of which coal-fired generation assistance is provided ***[Part 9, Division 4, clause 187]***. This test essentially requires the Authority to make an assessment of whether it is likely that the value of assistance provided in respect of a given asset under the Part will exceed the impact of the Scheme on the value of that asset (see 5.78 for more detail). The test requires a judgement of a windfall gain being 'likely', because such an assessment will be probabilistic rather than deterministic in nature. If, after consulting on a draft of its assessment in this regard, the Authority is satisfied that a windfall gain is likely, that is, the asset in question is assessed to pass the windfall gain test, the Authority must make a 'windfall gain declaration' in respect of that asset ***[Part 9, Division 4, clause 186(2)(a)].*** Conversely, if the Authority is not satisfied that the generation asset passes the windfall gain test, the Authority must not make a windfall gain declaration ***[Part 9, Division 4, clause 186(2)(b)]***.

5.62 A decision to make a windfall gain declaration, or to refuse to make a windfall gain declaration, in respect of a generation asset, will be subject to the review process in Part 24 of the draft bill. This allows affected persons to fully argue their position in respect of whether a windfall gain has in fact occurred. The significance of a windfall gain declaration is also such that the draft Australian Climate Change Regulatory Authority Bill 2009 prohibits such a decision from being delegated (Part 2, Division 5, clause 35(3)).

5.63 The draft bill clarifies that a windfall gain declaration is not a legislative instrument, and is therefore not subject to Parliamentary disallowance ***[Part 9, Division 4, clause 186(9)].*** This is appropriate as a windfall gain declaration is an administrative decision applicable to one entity, rather than a legislative decision of general application. Further, a windfall gain declaration is subject to both merits review (as noted above) and judicial review (for example, as provided by the *Administrative Decisions (Judicial Review) Act 1977*).

5.64 The second step of the windfall gain review provides the Minister administering the Act with discretion to make, or not make, a determination that prevents the issue of free Australian emissions units to a generation asset that is subject to a windfall gain declaration during the final two years for which coal-fired generation assistance is available. However, the Minister cannot make such a determination if a windfall

gain declaration is not in force in respect of this asset ***[Part 9, Division 4, clause 183(2)].***

5.65 The broad discretion afforded the Minister reflects the need for judgement as to whether withholding assistance under this clause would undermine the policy objective of providing assistance, or whether the provision of approximately three-fifths of the available assistance is likely to have proved effective in supporting that objective and withholding the remaining portion is a necessary measure to avoid providing the generation asset in question a windfall gain. As the Ministerial decision is in effect another form of review of the Authority's finding which already has an extensive merits review process, it would be inappropriate to subject it to another review process. Judicial review will remain available in respect of the Minister's decision, for example, as provided by the *Administrative Decisions (Judicial Review) Act 1977*.

5.66 The draft bill clarifies that a determination made by the Minister under this clause is not a legislative instrument, and is therefore not subject to Parliamentary disallowance ***[Part 9, Division 4, clause 183(5)].*** This is appropriate as a determination is an administrative decision applicable to one entity, rather than a legislative decision of general application.

5.67 If a windfall gain declaration is over-turned by a court or through a review process under Part 24, the Minister must revoke his or her determination to withhold assistance and the assistance withheld must be issued in a timely manner ***[Part 9, Division 4, clause 184].***

The effect of the review

5.68 The effect of a windfall gain declaration being made in respect of a generation asset is that no Australian emissions units are issued in respect of that asset for the last two of the five years for which assistance is provided under this Part ***[Part 9, Division 4, clause 183(1)]***. Accordingly, approximately two-fifths of the free Australian emissions units available in respect of any given generation asset are provided subject to the windfall gain review, whilst approximately three-fifths are provided without scope to be withheld under the review.

5.69 Part 9, Division 4 does not provide for part of the units that are subject to the windfall gain review to be withheld. The windfall gain review is not designed to allow a flexible amount of assistance to be withheld so as to provide the maximum possible number of free Australian emissions units while avoiding the occurrence of a windfall gain. Designing the review in this way would not reflect the inherent uncertainty in the extent of lost value for a given asset, and therefore the uncertain amount of assistance that would offset this loss whilst avoiding a windfall gain. Further, the intent of providing coal-fired generation

assistance was not to fully offset losses in asset value, but to partially offset extreme losses in order to support investor confidence in the sector. Within this context, the Minister will be able to consider, in respect of each individual generation asset, whether withholding the full amount of Australian emissions units that are subject to the review is appropriate where this will mean that the assistance provided falls significantly short of the loss of value in respect of that asset.

Information for the purposes of the review

5.70 The person issued units on 1 September 2012 must make a submission to the Authority about whether or not a windfall gain is likely ***[Part 9, Division 4, clause 185]***. This is to be in a form approved by the Authority and containing information and documents specified by the Authority in a legislative instrument. The Authority is best placed to determine what information will be required to apply the windfall gain test and so has been delegated the responsibility for setting these out in a legislative instrument. The *Legislative Instruments Act 2003* contains relevant provisions which govern the making of these instruments, including the consultation requirements set out in Part 3 of that Act.

5.71 The Authority will also be able to draw upon information from other regulatory bodies, such as the Australian Energy Regulator, through its information sharing provisions.

5.72 Failure to make a submission that complies with the necessary requirements will result in assistance being withheld ***[Part 9, Division 4, clause 185(4)]***.

The windfall gain test

5.73 As set out above, the windfall gain test essentially requires the Authority to make an assessment of whether it is likely that the value of assistance provided in respect of a given generation asset under the Part will exceed the loss of asset value experienced by that asset under the Scheme.

5.74 The extent of any loss of asset value experienced under the Scheme is to be assessed through a 'with or without analysis', that is, an analysis that looks at the value of the asset under the Scheme and its value in the event the Scheme was not implemented. The value of an asset will be primarily determined by looking at the revenue the asset is likely to earn over the period in question from generating electricity, and costs the asset is likely to incur in generating that electricity. The difference between the revenue of an asset and the costs it occurs in operating are described as the asset's 'net revenue' throughout Part 9, Division 4.

5.75 The Authority will perform the analysis over a 15 year period beginning on 1 July 2010, and consider both the effect of the Scheme and the effect of amending the *Renewable Energy (Electricity) Act 2000* to implement the Government's expanded national Renewable Energy Target ***[Part 9, Division 4, clauses 187(4)-(7)].*** As noted earlier, given the inherent uncertainties involved in such an analysis, the Authority's assessments of the extent to which an asset gains or loses value under the Scheme should be a broad, probabilistic assessment rather than the calculation of a single, precise value.

5.76 It is possible that the cost impact of the Scheme on a relatively less emissions-intensive coal-fired generator could be smaller than the increase in revenue enjoyed by that generator under the Scheme as its competitors face relatively larger increases in costs. This circumstance would result in an increase in the value of the asset under the Scheme. It is also possible that the increase in revenue enjoyed by a generator is approximately the same as the cost impact it faces, and that the asset is essentially indifferent to the introduction of the Scheme. If an asset is indifferent to the introduction of, or increases in value under, the Scheme, the provision of any assistance in respect of this asset can be considered to constitute a windfall gain. Accordingly, the Authority must firstly determine whether a generation asset (whether a generation complex or a generation complex project) is likely to experience a projected long-term net revenue gain ***[Part 9, Division 4, clauses 187(6) and 187(7)]***. Where an asset enjoys a 'projected long-term net revenue gain' under the Scheme, the asset is deemed to pass the windfall gain test ***[Part 9, Division 4, clause 187(2)(b)].***

5.77 Conversely, where the cost impact of the Scheme on a coal-fired generator is greater than the increase in revenue it enjoys under the Scheme, that generator will face a 'projected long-term net revenue loss'. The Authority must determine both whether a projected long-term net revenue loss is likely to occur for a generation asset (a generation complex or a generation complex project), and the extent of that projected long-term net revenue loss ***[Part 9, Division 4, clauses 187(4) and 187(5)]***.

5.78 Where an asset faces a projected long-term net revenue loss under the Scheme, the outcome of the windfall gain test relies on a comparison of the extent of this loss with the 'total value of assistance' provided in respect of that asset. The total value of assistance includes the value of assistance that has not yet been provided but will be provided subject to the windfall gain review ***[Part 9, Division 4, clause 187(3)].*** If the total value of assistance exceeds the projected long-term net revenue loss, the asset is deemed to pass the windfall gain test and therefore is subject to the Minister's power to make a determination withholding approximately two-fifths of the Australian emissions units that could be issued in respect of that asset. As noted earlier, the effect of such a

determination is to withhold all units that are subject to the review, which reflects the policy intent that providing coal-fired generation assistance was not to fully offset losses in asset value. The Government considers that partially offsetting extreme losses in asset value will be sufficient to support investor confidence in the electricity generation sector.

5.79 The total value of assistance provided in respect of a generation asset and the extent of a projected long-term net revenue loss or gain must be calculated in 'net present value' terms. That is, these losses or gains in value might occur at different points in time, and accordingly have a different impact on a notional investor. For example, a cost borne or a benefit received today has a greater impact on a notional investor as the money lost or received could be used for or deprived from an alternative purpose that provides a different stream of costs and benefits over time. To truly compare the impact of these changes in value on a notional investor, a net present value analysis 'discounts' costs and benefits that occur over a period of time to their value at the 'present' time. This calculation involves both a 'discount rate' and a point in time to use as the present. In this context, a discount rate is the extent to which a notional investor prefers to receive a benefit or avoid a cost today rather than in the future, so it can use the money received or cost avoided to make a new investment earlier rather than later, and earn a return on that investment earlier rather than later. To give greater certainty as to how these different elements of the net present value calculation will be performed, the Authority must publish a legislative instrument setting this out ***[Part 9, Division 4, clause 187(8)].***

5.80 Similarly, the Authority must set out how it will determine the market value and the projected market value of Australian emissions units ***[Part 9, Division 4, clause 187(8)]***, to clarify its calculation of the total value of assistance ***[Part 9, Division 4, clause 187(3)]***. For example, the instrument might set out how the Authority will use data relating to the trading of Australian emissions units on a public exchange to determine the market value or projected market value of these units. Finally, the Authority must set out how it will determine net revenue and projected net revenue for the purposes of determining whether there is a projected long-term net revenue loss or gain for an asset ***[Part 9, Division 4, clause 187(8)]***. For example, this instrument might set out what costs will be deducted from the revenue of a generation asset to determine its net revenue or projected net revenue.

5.81 The Government has set out that the Authority's considerations in the windfall gain test should incorporate the effect of contracts entered into prior to 3 June 2007. Such contracts, where they allow a generation asset to pass a greater portion of its costs under the Scheme onto its customers than its economic position in the market might otherwise allow, could increase the likelihood of a generator receiving a windfall gain

through the Electricity Sector Adjustment Scheme. Accordingly, the legislative instrument will set out how the Authority must take these contracts into account when setting out how it will calculate the net revenue or projected net revenue of generation assets ***[Part 9, Division 4, clause 187(9)].*** The Government expects that this instrument will set out how the Authority will assess the extent of carbon cost pass through under particular contracts, and adjust the net revenue and projected net revenue calculations for generation assets in light of this and other elements of contracts.

5.82 However, the extent of the matter is limited to the specific consideration of individual contracts entered into before 3 June 2007. The Authority should take into account the general market value of electricity sold by generators in assessing the net revenue and projected net revenue of generators under the windfall gain test. This assessment should be informed by considering prevailing prices for electricity reflected in hedge contracts or direct supply contracts entered into after 3 June 2007. However, such contracts have been, and will be, made with full knowledge of the potential impact of the Scheme on the respective parties to the contract. The intent is that the Authority would not take into account the specific terms of individual contracts entered into after 3 June 2007, but should not be limited from considering the general level of electricity prices as revealed through activity in markets for hedge contracts or direct supply contracts. This approach does not give generators an incentive to enter into disadvantageous or perverse contractual arrangements to distort the effect of the windfall gain review, whilst allowing the Authority to generally consider revealed prices in contract markets as a useful input into its assessments of net revenue and projected net revenue.

5.83 If, in undertaking a windfall gain test, the Authority took into account the fact that the owner of that asset had, for example, modified the asset to improve its efficiency, or planned to do so, its calculation of the projected long-term net revenue loss of the asset would be likely to be lower (reflecting its improved efficiency) and therefore would be more likely to be less than the value of assistance provided in respect of that asset. Therefore, if actual, planned or possible upgrades to generation assets were taken into account as part of the windfall gain test, the test itself would discourage efficiency improvements or other modifications to generation assets that might reduce emissions of greenhouse gases. This, in turn, would undermine the overall objective of the Scheme. Therefore, the Authority is required not to take these into account in undertaking the windfall gain test ***[Part 9, Division 4, clauses 187(11) and 187(12)]***.

5.84 The legislative instrument setting out these matters will be subject to the requirements of the *Legislative Instruments Act 2003*, including the consultation requirements in Part 3 of that Act.

5.85 In undertaking the windfall gain test, the Authority is required to assume that all Australian emissions units are issued in respect of each generation asset ***[Part 9, Division 4, clause 187(13)]***. This is because the windfall gain test is designed to consider what the impact of the Scheme, and the assistance provided under this Part, would be if the full amount of Australian emissions units available in respect of each generation asset were issued to that asset. The windfall gain test is not designed to consider what will happen in the event that units are withheld under the windfall gain review or the power system reliability test (which is set out in Part 9, Division 5). If this approach were adopted, the windfall gain review would become circular.

Power system reliability test

5.86 The Government has designed the provision of assistance to coal-fired generators under this Part in a way that minimises the risk of giving recipients incentives to change their future production decisions to increase the amount of assistance they will receive. However, in response to stakeholder views, the Government has decided to impose a limited form of conditionality on the provision of assistance that may alter the decisions of some owners, operators or controllers of generation assets in respect of which assistance is available to withdraw generating capacity from Australia's electricity markets.

5.87 Part 9, Division 5 requires generation assets to comply with the 'power system reliability test' in order to receive assistance available under this Part. This creates an incentive for owners, operators or controllers of generation assets (specifically, those in respect of which assistance is available) to comply with the power system reliability test, which in turn reduces the risk of unexpected behaviour impacting on the reliability of supply in Australia's electricity markets. An example of such unexpected behaviour might be where the reduction in asset value of a generator causes its financiers to force a generator to shut down even though it is still required to operate to maintain sufficient supply in an electricity market.

5.88 The power system reliability test does not apply to generation complex projects ***[Part 9, Division 5, clause 188]***. Although assistance can be provided in respect of generation complex projects, generation assets that were found to be eligible for coal-fired generation assistance as a generation complex project may, as a matter of fact, satisfy the definition of a generation complex at some point in time prior to the final issue of free Australian emissions units under this part on 1 September 2014. At that point in time, the generation asset would satisfy ***[Part 9, Division 5, clause 188(1)(b)]*** and therefore become subject to the power system reliability test,

regardless of the fact that it received assistance on the basis of eligibility as a generation complex project.

5.89 Free Australian emissions units are not to be issued in respect of a generation complex where it does not meet the power system reliability test ***[Part 9, Division 5, clause 188]***. This test must be applied to each generation complex individually each time Australian emissions units are issued in respect of that asset ***[Part 9, Division 2, clause 176(2) and 176(9)]***.

5.90 The power system reliability test is structured around concepts and processes established outside the draft bill in laws relating to the regulation of energy markets ***[Part 9, Division 5, clause 189]***. The primary laws (and instruments made under those laws) that are likely to be applied in the Authority's assessments of the power system reliability test are:

- in relation to the National Electricity Market, the National Electricity Rules
- in relation to the Western Australian Wholesale Electricity Market, the Wholesale Electricity Market Rules.

5.91 These laws require generators to register with the operator of the energy market in which they operate. Rule 2.2 of the National Electricity Rules requires the person who engages in the activity of owning, controlling or operating a generator in the National Electricity Market to register with the National Electricity Market Management Company (NEMMCO), unless it is the subject of an exemption. Similarly, Regulations 14 and 19 of Western Australia's *Electricity Industry (Wholesale Electricity Market) Regulations 2004* require a person who engages in the activity of owning, controlling or operating a generator in the Western Australian Wholesale Electricity Market to register with the Independent Market Operator of Western Australia, subject to exemptions and a minimum capacity requirement. Registration as a generator under these two laws requires compliance with a range of technical and operational conditions. In turn, compliance with these conditions supports the reliable and safe operation of the National Electricity Market and Western Australian Wholesale Electricity Market, and gives NEMMCO and the Independent Market Operator of Western Australia powers necessary to manage system security.

5.92 Accordingly, the power system reliability test supports the reliable and safe operation of the National Electricity Market and Western Australian Wholesale Electricity Market by using the value of assistance available under this Part to create incentives that impact on the circumstances under which a recipient of assistance will cease its registration as a generator, or reduce its registered 'nameplate rating'. A generation complex's nameplate rating is its maximum continuous

electrical output and as registered with the appropriate energy market operator. Schedule 3.1 of the National Electricity Rules requires a scheduled generator to register its full generating load in megawatts for each 'generating unit', and its 'total station registered capacity' in megawatts with NEMMCO. Similarly, clause (b)(ii) of Appendix 1 of the Western Australian Wholesale Electricity Market Rules requires a scheduled generator to register its nameplate capacity in megawatts with the Independent Market Operator of Western Australia. Numbers registered in accordance with these requirements can be considered to represent the nameplate rating of a given generation complex, which in turn represents the amount of generation capacity that is subject to the conditions of registration.

5.93 The power system reliability test focuses on changes to a generation complex's nameplate rating because the reliability of a power system depends, in part, on the maximum continuous electrical output of all the generators connected to the system being sufficient to supply the maximum likely demand for electricity within the system, whilst also allowing for contingencies such as malfunctions of generators and technical constraints on the safe operation of the system. Both the National Electricity Rules and the Western Australian Wholesale Electricity Market Rules set out various power system reliability standards. Under both laws, the particular standard that is most likely to be affected by changes to a generation complex's nameplate rating is the 'medium term projected assessment of system adequacy'. NEMMCO and the Independent Market Operator of Western Australia are required to undertake a medium term projected assessment of system adequacy on a regular basis under rule 3.7.2 of the National Electricity Rules and rule 3.16 of the Western Australian Wholesale Electricity Market Rules respectively.

5.94 A generation complex will pass the power system reliability test if the nameplate rating of that generation complex remains the same as, or exceeds, the level it was on 3 June 2007 ***[Part 9, Division 5, clauses 189(2)(a) and 189(2)(b)]***. Under this circumstance, the generation complex in respect of which assistance is provided under this Part has not reduced its maximum continuous generation capacity, and so has not reduced its ability to contribute to satisfying the maximum likely demand for electricity within the system. Further, the generation complex that is registered with this capacity is, through the act of remaining registered, required to comply with technical and operational requirements that improve the likelihood that it will be physically capable of supplying that amount of electricity at times of high demand when it is most required. Breaches of the power system reliability standards cannot be reasonably attributed to the actions of generation complexes that comply with either ***[Part 9, Division 5, clause 189(2)(a)]*** or ***[Part 9, Division 5, clause 189(2)(b)]***, but are

more likely to be due to insufficient investment in new generation capacity to satisfy growth in demand for electricity.

5.95 It is possible that the Scheme will change the relative cost of different generators within a given energy market such that the owner, operator or controller of a generation complex will seek to retire all or part of that generation complex from service. A retired generation unit or generation complex would be unlikely to comply with the range of conditions required as part of remaining registered. Accordingly, the owner, operator or controller would be likely to seek to reduce its registered nameplate rating, or to cease its registration entirely, under such a circumstance.

5.96 It is unlikely that a generator would seek to reduce its registered nameplate rating or cease its registration at a time when the supply of generation capacity was low relative to demand in the system. Such a circumstance would be likely to correspond with a period of high prices for electricity (in the National Electricity Market) or for 'capacity credits' in the Western Australian Wholesale Electricity Market, which would reduce the incentive to exit the market. However, as noted earlier, the power system reliability test is designed to guard against unexpected behaviour reducing the reliability of supply in Australia's electricity markets.

5.97 Therefore, the power system reliability test allows a generator to reduce its nameplate rating where there is unlikely to be a breach of applicable power system reliability standards within two years after that event, taking into account the reduction in generation capacity from the asset in question ***[Part 9, Division 5, clause 189(2)(c)]***. The power system reliability test also allows a generator to cease its registration where there is unlikely to be a breach of applicable power system reliability standards within two years, taking into account the removal of the generation capacity of the asset in question from the market ***[Part 9, Division 5, clause 189(2)(d)]***.

5.98 The technical assessments that underpin this element of the power system reliability test are best performed by the relevant energy market operator, that is, NEMMCO in relation to the National Electricity Market and the Independent Market Operator of Western Australia in relation to the Western Australian Wholesale Electricity Market, rather than the Authority. For this reason, the Authority is required to rely on an appropriate certification by the relevant energy market operator, rather than on its own judgement of the circumstances ***[Part 9, Division 5, clauses 189(2)(c) and 189(2)(d)]***. These provisions do not place a formal power on the relevant energy market operators, but require owners, operators or controllers of generation assets in respect of which assistance is provided to obtain appropriate documentation from NEMMCO or the Independent

Market Operator of Western Australia to the satisfaction of the Authority in the event that they wish to cease their registration or reduce the registered nameplate rating of that asset.

5.99 The term 'appropriate energy market operator' is intended to capture proposed changes to the operator of the relevant energy markets, including the proposed replacement of NEMMCO with the Australian Energy Market Operator ***[Part 9, Division 5, clause 189]***.

Chapter 6
Reforestation

Outline of chapter

6.1 This Chapter describes the rules for issuing free Australian emissions units for eligible reforestation projects which are contained in Part 10 of the draft bill. The Chapter also sets out the circumstances in which emissions units must be relinquished and the rules for maintaining forests if units are not relinquished.

Context

6.2 Forests sequester carbon dioxide as they grow. Issuing free units, in addition to the Scheme cap, for net increases in greenhouse gas removals creates an incentive for reforestation. It will also allow the Scheme cap to be achieved at lower cost than would otherwise be possible.

Summary of reforestation scheme

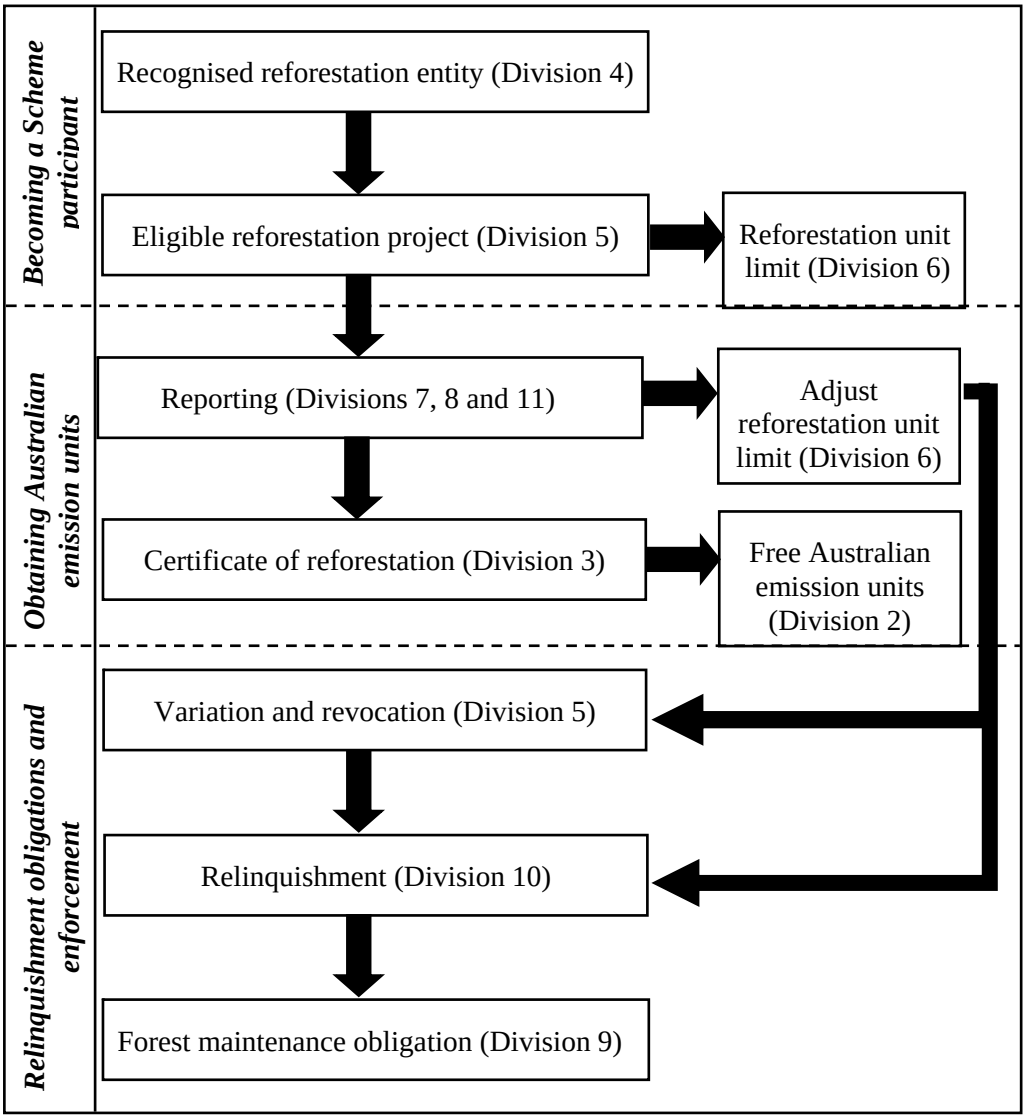
6.3 A recognised reforestation entity may apply to the Authority for the issue of a certificate of reforestation that entitles the entity to receive free units for net increases in greenhouse gas removals from an eligible reforestation project ***[Part 10, Division 3, clause 192]***. Provided all relevant requirements under the reforestation scheme in Part 10 have been met, such a certificate will be issued to the entity.

6.4 A certificate of reforestation is issued, broadly, on the basis that the entity is the holder of the 'carbon sequestration right' in relation to an eligible reforestation project that meets scheme requirements and has reported a net increase in greenhouse gas removals resulting from the project.

6.5 The Authority will issue a notice of relinquishment if units have been issued in excess of the unit limit for the project or if the recognised reforestation entity, in effect, withdraws the project from the scheme ***[Part 10, Division 10, clauses 232, 233]***.

6.6 If the requisite number of units is not relinquished by the recognised reforestation entity, generally the land on which the reforestation project was carried out will become subject to a forest maintenance obligation. This obligation is to manage and maintain the forest such that the amount of net greenhouse gas removals when the forest is mature is equivalent to the total number of units that have been issued in respect of the reforestation project less any units that have been relinquished ***[Part 10, Division 10, clause 226]***.

6.7 The following diagram provides a broad outline of the various requirements and processes involved in the reforestation scheme under Part 10. Part 10 also includes a simplified outline ***[Part 10, Division 1, clause 190].***



Detailed explanation of reforestation scheme

Becoming a scheme participant

Recognised reforestation entities

6.8 A person must be a 'recognised reforestation entity' to participate in the reforestation scheme under Part 10 of the draft bill.

Application process

6.9 A person (whether an individual, a body corporate or a body politic such as a State or a Territory) may apply to the Authority to become a recognised reforestation entity ***[Part 10, Division 4, clause 198]***.

6.10 The regulations will specify any information or documents that will be required to accompany an application ***[Part 10, Division 4, clause 199]***.

6.11 The Authority may by written notice require an applicant to provide additional information that the Authority considers necessary to enable a decision to be made on an application. Where that information is not provided within the time frame specified in the notice the Authority may refuse to consider or take any further action in relation to the application ***[Part 10, Division 4, clause 200]***.

6.12 The regulations may specify an application fee ***[Part 10, Division 4, clause 199].*** The purpose of the fee is to enable the Authority to recover costs associated with processing the application. An application fee is considered appropriate given that participation in the reforestation scheme under Part 10 will be voluntary, open to any entity, and will deliver financial benefits. Moreover, the Authority will incur costs in the process of determining whether the person is a 'fit and proper person'.

6.13 The Authority must take all reasonable steps to ensure that a decision is made on the application within 90 days of the making of the application or, where relevant, the receipt of further information. If the Authority refuses the application, the applicant must be given written notice of this ***[Part 10, Division 4, clause 201]***.

Criteria for recognition

6.14 The Authority may recognise the applicant as a reforestation entity if satisfied that, among other things, the applicant is a fit and proper person. In making this assessment the Authority must have regard to matters that include any convictions the applicant has under a law of the Commonwealth, a State or a Territory relating to dishonest conduct,

breaches by the applicant of the Scheme legislation or the associated provisions and any other matters the Authority considers relevant. The Authority must also have regard to any orders made by the Australian Competition and Consumer Commission under section 76 of the *Trade Practices Act 1974* in relation to business dealings by the applicant. In addition, the Authority must be satisfied that the applicant, where an individual, is not an insolvent under administration or, where a body corporate, is not under external administration ***[Part 10, Division 4, clause 201]***.

6.15 The regulations may specify additional criteria, such as a requirement that the applicant has some other type of approval or licence under a Commonwealth, State or Territory law that is relevant to reforestation.

6.16 The application of a fit and proper person test seeks to minimise the risk of any fraudulent, deceptive or unfair conduct by entities involved in the reforestation scheme.

6.17 The Authority will have the power to cancel a person's recognition as a reforestation entity where the Authority is no longer satisfied that the person remains a fit and proper person, assessed against the same criteria as for recognition, or no longer meets one or more other requirements ***[Part 10, Division 4, clause 202]***.

6.18 A person may surrender their recognition as a reforestation entity by written notice to the Authority ***[Part 10, Division 4, clause 203]***.

6.19 If an entity is a recognised reforestation entity, the entity's recognition is not transferable ***[Part 10, Division 4, clause 204]***.

Eligible reforestation projects

6.20 Under the reforestation scheme in Part 10, free units can only be obtained in respect of a reforestation project that has been declared by the Authority, under clause 209, to be an 'eligible reforestation project'. A declaration that a proposed project is an eligible reforestation project can only be made if the proposed project meets the requirements of the scheme. A declaration made under clause 209 must identify the 'project area' or areas involved in the project - that is, the area or areas of land on which the project will be carried out - and any other project attributes as may be specified in the regulations ***[Part 10, Division 5, clause 209]***.

Application process

6.21 A person may apply to the Authority to have a reforestation project declared to be an eligible reforestation project ***[Part 10, Division 5, clause 205]***.

6.22 The regulations will specify any information and documents that must accompany an application ***[Part 10, Division 5, clause 206]***.

6.23 The Authority may by written notice require an applicant to provide additional information that the Authority considers necessary to make a decision on an application. Where that information is not provided within the time frame stated in the notice the Authority may refuse to consider or take any further action in relation to the application ***[Part 10, Division 5, clause 207]***.

6.24 An application can be withdrawn at any time before the Authority has made a decision on the application ***[Part 10, Division 5, clause 208].*** This might occur where, after an application has been made, it is considered that changes should be made to the proposed project to ensure Scheme eligibility requirements will be satisfied.

6.25 If an application is withdrawn, the Authority is required to refund any application fee that has been paid ***[Part 10, Division 5, clause 208]***.

6.26 The withdrawal of an application does not prevent the applicant from making a fresh application in relation to the same or a similar project ***[Part 10, Division 5, clause 208]***.

6.27 The Authority must take all reasonable steps to ensure that a decision is made on the application within 90 days. If a declaration is made, the Authority must give the applicant a copy of it. If the Authority decides to refuse to make the declaration sought, the applicant must be notified of this in writing ***[Part 10, Division 5, clause 209]***.

Criteria for declaration

6.28 An application for a declaration of an eligible reforestation project must relate to a 'reforestation project'. The term 'reforestation project' is defined to mean a project for the establishment, management and maintenance of one or more 'forest stands' or the management and maintenance of one or more existing forest stands ***[Part 1, clause 5, definition of 'forest stand']***.

6.29 The definition of 'forest stand' in clause 5 of the draft bill incorporates the various elements of Australia's definition of a forest for reforestation and afforestation purposes under the Kyoto Protocol. A 'forest stand' is a stand of forest that:

- has been established by direct human induced methods (as defined in the regulations)
- has trees with a potential height of at least two metres

- has trees with a potential crown cover of at least 20 percent of the area occupied by the stand
- occupies an area of land of 0.2 hectares or more
- is on land that, as at 31 December 1989, was clear of trees with a potential height of at least two metres and a potential crown cover of at least 20 percent
- meets any other requirements specified in regulations.

6.30 It is envisaged that the regulations will specify requirements going to the calculation and reporting of net greenhouse gas removals, including that the trees comprising a forest stand be established at the same time within a single encompassing boundary (and excluding all non forest stand areas) and are of the same (set of) species and are subject to the same management regime.

6.31 The Authority may declare that a reforestation project is an 'eligible reforestation project' provided that certain requirements are met:

- the applicant must be a recognised reforestation entity
- the applicant must hold the 'carbon sequestration right' in relation to the project (in essence, the exclusive legal right to obtain the benefit of carbon sequestration by the forest stand or stands involved in the reforestation project)
- the 'project area' or areas (i.e. the land on which the project is to be carried out) must be freehold Torrens system land, or Crown land (whether or not Torrens system land)
- the project area or areas cannot be general law land (i.e. land that is neither freehold nor Crown land), or land that is excluded by the regulations
- if the project is to be carried out on State or Territory Crown land (and the applicant for the declaration is not the Crown), the State or Territory must have certified that the applicant holds the 'carbon sequestration right' in relation to the project, and that the land in question will not be dealt with in a way that would defeat or otherwise be inconsistent with that right
- the project must satisfy any other eligibility requirements specified in the regulations

- the holders of certain kinds of interests in the land on which the project is to be carried out must have consented to the making of the application for the declaration of the reforestation project ***[Part 10, Division 5, clause 209]***.

6.32 The consent of certain other interest holders is a precondition to the declaration of a project as an eligible reforestation project because, in some limited circumstances, an area of land involved in a project can become subject to the forest maintenance obligation (explained in paragraphs 136 - 140 below). Depending on the circumstances, that obligation may have to be satisfied by a person other than the applicant for the declaration of a project as an 'eligible reforestation project'. Therefore, it is important to ensure that any person who might become responsible for satisfying the forest maintenance obligation, or whose interest in the land might be affected by that obligation, has agreed to the land being brought into the reforestation scheme.

6.33 The need to obtain the consent of other relevant interest holders creates an opportunity for negotiation between the person who would obtain a direct benefit under the scheme (i.e. the applicant for the declaration) and those other interest holders.

Example 6.1 Consent of farmer

A farmer has the freehold in an area of land. Five years ago he granted a lease over the land for a certain price.

The lessee wants to bring a reforestation project on the leased land into the reforestation scheme (by having it declared to be an 'eligible reforestation project'). She needs to obtain the farmer's consent to do this.

As the farmer could potentially become subject to the forest maintenance obligation, he might refuse to give consent to this.

Alternatively, the farmer might give consent in return for a fixed sum, or a proportion of any units that might be issued, under the scheme, in respect of the reforestation project.

6.34 The provisions setting out the criteria for declaring a project to be an 'eligible reforestation project' are still under consideration and require further development in two areas in particular.

6.35 First, clause 209(4)(b) currently has the effect that, if a reforestation project is to be carried out on Torrens system land, the project must be confined to an area of land held under a single title. However, it is envisaged that this requirement will be removed from the draft bill. This change will require amendment of a number of provisions

in Part 10. For example, the bill will need to provide for unit limits and unit entitlements to be calculated separately for each forest stand involved in an eligible reforestation project and then aggregated for the project. Provisions in relation to the forest maintenance obligation will be amended so that, in relevant cases, the obligation can apply to discrete project areas rather than applying in all cases to all project areas involved in the project. Provision will also be made to allow the transfer of a carbon sequestration right in relation to part of a project.

6.36 The second aspect of these provisions that is still under consideration is what criteria should apply where a reforestation project would be carried out on land granted under Commonwealth, State or Territory land rights legislation (or held for the benefit of Aboriginal peoples or Torres Strait Islanders under Commonwealth, State or Territory legislation), and land subject to native title rights. Further provisions will be included in the bill to address these matters.

When a declaration takes effect

6.37 A declaration made under clause 209 takes effect either immediately after it is made or, with the applicant's consent, on an earlier date specified in the declaration. The declaration cannot take effect before 1 July 2010, and cannot be backdated more than 5 years prior to the day on which the application was made ***[Part 10, Division 5, clause 209].***

6.38 Australian emissions units can be issued for net greenhouse gas removals from the date that the eligible project declaration takes effect. Allowing a declaration to be backdated gives small forest growers time to assess the merits of scheme participation following forest establishment.

Forestry right

6.39 Clause 241 defines the term ‘forestry right’, for the purposes of the draft bill. In order to be the holder of the ‘forestry right’ in relation to a reforestation project, a person must have a legal estate or interest in the area of land on which the project is (or is to be) carried out which gives the person the exclusive legal right to establish, maintain and manage - including harvest - a forest on that area of land ***[Part 10, Division 14, clause 241].***

6.40 Under the draft bill, only a proprietary estate or interest in land can result in the holder having a ‘forestry right’ - a personal right, such as a licence or a mere contractual right, is not enough. It should be noted, however, that some State legislation deems certain forestry-related rights to be estates or interests in land, and rights that are subject to such legislation can be ‘forestry rights’, for the purposes of the draft bill.

6.41 Various kinds of estates or interests in an area of land may give a person the 'forestry right' in relation to a reforestation project carried out on that area. For example:

- in relation to an area of Torrens system freehold land, the person who holds the estate in fee simple will have the forestry right unless he or she has granted to another person an interest in the land (such as, for example, a lease) which gives them that right;

- a lease over an area of Torrens system freehold land under which the lessee has exclusive possession of the area will generally give the lessee the forestry right (unless the lessee has granted it to someone else - for example, a sublessee);

- where a reforestation project is carried out on Crown land in a State or Territory, the State or Territory itself will hold the forestry right in relation to the project, unless that right has been granted to someone else (for example, under a lease).

6.42 In a case where the land on which a person carries out a reforestation project is Torrens system land, the person's estate or interest in the land will only be a 'forestry right' if it is registered on the certificate of title.

6.43 It is important to realise that the reforestation scheme in Part 10 does not itself create forestry rights (or any other kind of rights) in relation to land. Rather, the legislation simply sets out the characteristics that a right held by a person must have in order to be a 'forestry right', for the purposes of the reforestation scheme.

Carbon sequestration right

6.44 The concept of a 'carbon sequestration right' is central to the operation of the reforestation scheme in Part 10 of the draft bill. This is because, under that Part, the only person who can obtain free units in respect of an eligible reforestation project is the person who holds a right that comes within the definition of 'carbon sequestration right'.

6.45 It should be noted that, as with forestry rights, the legislation will not itself create carbon sequestration rights. Rather, the scheme will enable a recognised reforestation entity to obtain free units in respect of an eligible reforestation project if the entity already has the carbon sequestration right in relation to the project. In other words, being the holder of the carbon sequestration right is a prerequisite to a recognised entity's participation in the reforestation scheme.

6.46 A person will only hold the carbon sequestration right in relation to an eligible reforestation project if the person holds a particular kind of right in relation to the area or areas of land on which the project is (or is to be) carried out. The definition in clause 240 sets out the characteristics a right must have in order to be a 'carbon sequestration right', for the purposes of the draft bill ***[Part 10, Division 14, clause 240].***

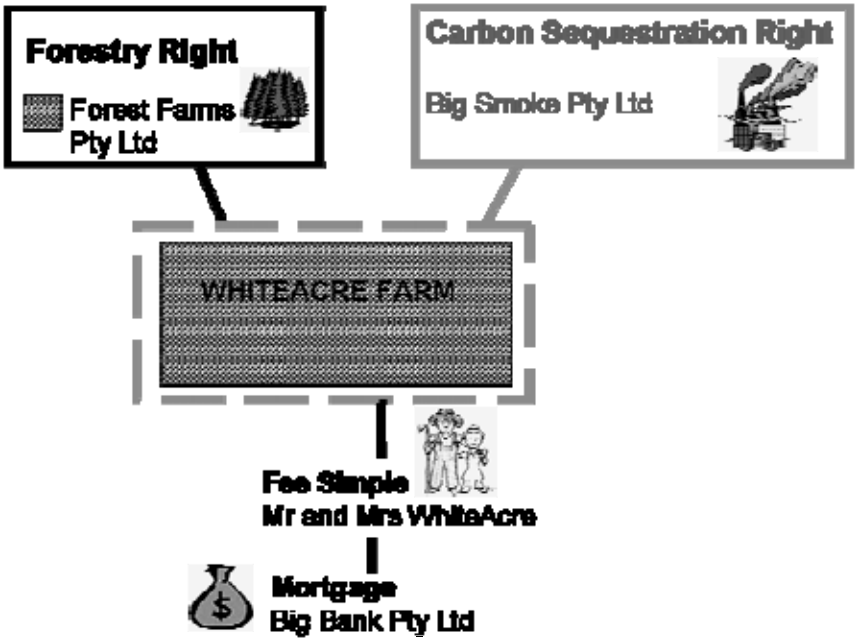
6.47 In essence, a carbon sequestration right is the exclusive legal right to obtain the benefit of sequestration of carbon dioxide by trees to which an eligible reforestation project relates. As with a forestry right, various kinds of estates or interests in land on which eligible reforestation projects may be carried out can give the holder of the estate or interest the exclusive legal right to obtain that benefit. For example:

- in relation to an area of Torrens system freehold land, the holder of the estate in fee simple will have the carbon sequestration right unless he or she has granted to another person an interest in the land (such as, for example, a lease) which gives them that right

- a lease over an area of Torrens system freehold land under which the lessee has exclusive possession of the area will generally give the lessee that right.

6.48 It is likely that, in many cases, the person who holds the forestry right in relation to an eligible reforestation project will also be the holder of the carbon sequestration right. For example, a person who is to carry out an eligible reforestation project on an area of land might do so under a lease which gives the person the right to establish, maintain and manage a forest on that land - that is, the 'forestry right' in relation to the project. Unless the lessee has granted to another person the exclusive legal right to obtain the benefit of carbon sequestration by trees involved in the project, the lessee will be the holder of the 'carbon sequestration right'.

6.49 However, the definition of 'carbon sequestration right' also allows for the possibility that that the two rights might be separated and held by different persons. The diagram below (adapted from a diagram provided by Landgate, Government of Western Australia) illustrates a range of property rights that can exist with respect to an area of land.



6.50 There are, however, certain requirements that must be satisfied in a case where the holder of the carbon sequestration right does not also hold the forestry right. First, if the right relates to an area of Torrens system freehold land, the right must be registered on the certificate of title. The right must also be one that runs with the land - that is, it must be such that successors in title to estates or interests in the land will take those estates or interests subject to that right. If a carbon sequestration right itself arises from an estate or interest in the land in question - for example, a registered lease - then, by virtue of the State or Territory Torrens system legislation, it will run with the land. But, in certain cases, such a right may run with the land even if it is not an estate or interest in the land. This will be so in a case where State or Territory carbon property rights legislation deems the right to be such an estate or interest in land, or otherwise has the effect that such a right runs with the land.

6.51 It should be noted that, while Part 10 of the draft bill will allow for eligible reforestation projects to be carried out on Torrens system land and Crown land (whether Torrens system land or not), the reforestation scheme will not apply so as to allow a person to obtain free units in respect of projects carried out on general law land, i.e. land that is neither Torrens system land nor Crown land. (State and Territory legislation provides for the conversion of general law land to Torrens title land.)

6.52 The definitions of 'forestry right' and 'carbon sequestration right' are still being developed at this stage, and additional provisions will be included in the bill as introduced. Issues that will be addressed in these further provisions include the application of the reforestation scheme in

relation to land granted under Commonwealth, State or Territory land rights legislation (or held for the benefit of Aboriginal peoples or Torres Strait Islanders under Commonwealth, State or Territory legislation), and land subject to native title rights.

Reforestation unit limit

6.53 As soon as practicable after declaring a project to be an eligible reforestation project, the Authority will issue to the carbon sequestration right holder a notice specifying the reforestation unit limit for the project ***[Part 10, Division 6, clause 220].***

6.54 The unit limit represents the maximum total number of units that can be issued, over time, in respect of an eligible reforestation project.

6.55 The unit limit will be based, in part, on a calculation undertaken by a computer program of net greenhouse gas removals resulting from the individual forest stands within the project. It is intended that, in accordance with the regulations, this calculation will be based on an average of cumulative net greenhouse gas removals over the time period specified in regulations. These regulations may be amended from time to time, following a period of notice, to reflect changes in the accounting rules and the estimation methodology.

6.56 To enable the calculation of the unit limit, the carbon sequestration right holder will be required to provide information on:

- forest management actions, intended and actual (e.g. forest establishment date, species planted and any harvesting events).
- natural disturbances such as fire and wind-throw (if and when they occur).

6.57 The calculation of the unit limit will also take into account the 2008 carbon stock baseline for the project and any sale of abatement from the reforestation project to schemes or projects outside of the Carbon Pollution Reduction Scheme.

6.58 The unit limit for an eligible reforestation project can be increased ***[Part 10, Division 6, clause 221]*** or decreased ***[Part 10, Division 6, clause 222]*** to reflect changes in circumstances resulting in an increase or decrease in net greenhouse gas removals arising from the project.

6.59 The Authority will notify the carbon sequestration right holder where there are any changes to the unit limit ***[Part 10, Division 6, clause 221, 222].***

Decision by a computer program

6.60 The Authority will have the capacity to make use of a computer program for the purpose of working out the reforestation unit limit ***[Part 10, Division 6, clause 220].***

6.61 It is envisaged that the computer program used for this purpose will incorporate an updated version of the National Carbon Accounting Toolbox.

6.62 It is intended that further provisions will be included in the bill to enable a carbon sequestration right holder to apply for modifications to be made to aspects of the parameter values underlying the computer program including in relation to calculation of the unit limit.

Obtaining Australian emissions units

Reforestation reports

6.63 The recognised reforestation entity who is also the carbon sequestration right holder in respect of an eligible reforestation project must submit a reforestation report to the Authority in the manner and form specified by regulations ***[Part 10, Division 8, clause 225].***

6.64 It is intended that the regulations will specify that reports will be required to include the data relevant for the operation of the National Carbon Accounting Toolbox, for example, information on forest establishment date, forest species, harvesting and thinning schedules (if any) and natural disturbance events (if any).

6.65 The regulations will specify that reforestation reports need to include information on all forest stands included in the reforestation project.

6.66 It is envisaged that further provisions will be included in the bill requiring reporting in relation to emissions (above a specified threshold) arising from certain actions or events - for example, management actions such as unplanned harvesting, or significant natural disturbances affecting forests involved in an eligible reforestation project.

6.67 The Australian Climate Change Regulatory Authority Bill will include provisions requiring periodic auditing of information provided in reforestation reports. It is intended that reforestation entities have their reforestation reports audited at least every five years whilst their forests are still eligible to receive units.

6.68 Registration of auditors, audit requirements and other related issues will be contained in the Australian Climate Change Regulatory Authority Bill and will apply consistently to all Scheme participants.

Reforestation reporting periods

6.69 The person who holds the carbon sequestration right in relation to an eligible reforestation project must submit the first reforestation report in respect of the project within 5 years but not earlier than 12 months after the project was declared to be eligible ***[Part 10, Division 7, clause 223].***

6.70 Subsequent reforestation reports must be submitted within 5 years but not earlier than 12 months after the previous report was submitted ***[Part 10, Division 7, clause 224].***

6.71 A reporting period for a project does not need to be nominated in advance. A reporting period is, in effect, nominated when a report is submitted ***[Part 10, Division 7, clauses 223, 224]***.

Issue of Australian emissions units

6.72 The Authority will issue to the holder of a certificate of reforestation the number of free Australian emissions units specified in the certificate. Units will be issued as soon as practicable after the certificate has been issued.

6.73 The financial year in which the units are issued will be the vintage year of the units.

6.74 Units can only be issued if the entity has a Registry account ***[Part 10, Division 2, clause 191]***.

Certificate of reforestation

6.75 A certificate of reforestation specifies the number of free Australian emissions units that will be issued to the certificate holder.

6.76 Under the reforestation scheme, only recognised reforestation entities will be eligible to apply for a certificate of reforestation ***[Part 10, Division 3, clause 195]***.

6.77 A certificate of reforestation is not transferable ***[Part 10, Division 3, clause 197]***.

Application process

6.78 An application for a certificate of reforestation can be made if the entity has submitted a reforestation report to the Authority - that is, a report relating to an eligible reforestation project ***[Part 10, Division 3, clause 192]***.

6.79 Additional provisions may be included in the bill to allow the regulations to specify an application fee. The purpose of the fee is to enable the Authority to recover costs associated with processing the application.

6.80 An application must be in a form approved by the Authority ***[Part 10, Division 3, clause 193]***.

6.81 An application may be set out in the same document as the reforestation report ***[Part 10, Division 3, clause 192]***.

6.82 It is anticipated that all Scheme documents will be available, and able to be completed and submitted electronically, via the internet.

6.83 The Authority may by written notice require an applicant to provide additional information that the Authority considers necessary to make a decision on an application. Where that information is not provided within the time frame specified in the notice, the Authority may refuse to consider or take any further action in relation to the application ***[Part 10, Division 4, clause 194]***.

6.84 The Authority must take all reasonable steps to ensure that a decision is made on the application within 90 days of being given the application or, where relevant, further information. If the Authority refuses to issue a certificate, written notice of this must be given to the applicant ***[Part 10, Division 4, clause 195]***.

6.85 Where a person has applied for a certificate of reforestation, section 136.1 of the *Criminal Code* will apply in relation to statements made in the associated reforestation report ***[Part 10, Division 3, clause 192]***. Section 136.1 of the *Criminal Code* is concerned with the making of false or misleading statements in or in connection with certain kinds of applications.

Criteria for issuance

6.86 Following submission of a reforestation report, the Authority must issue the certificate if the following conditions are met:

- the Authority is satisfied that the applicant is a recognised reforestation entity and has the 'carbon sequestration right' in relation to the eligible reforestation project
- the applicant is not subject to a requirement under Part 10 to relinquish units issued in relation to a reforestation project
- the applicant is not subject to an outstanding requirement to pay an administrative penalty in relation to a reforestation project
- over the period covered by the report, the reforestation project has resulted in a net increase in greenhouse gas removals of at least one tonne
- the total net total number of tonnes of greenhouse gases removed by the project are greater than the net total number of units issued in respect of the project
- units have not yet been issued up to the unit limit for the project
- the Authority is satisfied that, if the regulations specify any additional eligibility requirements, those requirements have been met.

[Part 10, Division 3, clause 195]

6.87 Regulations will specify the way in which the 'net total number of tonnes of greenhouse gases removed' as a result of a reforestation project is to be worked out, which will involve the application of a formula. Clause 195(8) authorises the making of regulations providing for a number that is a component of such a formula to be worked out using a computer program. It is intended that the Authority will use the National Carbon Accounting Toolbox for this purpose.

6.88 The net total number of units issued in respect of the reforestation project is calculated by subtracting from the total number of units that have been issued for the project less the total number of units that have already been relinquished in relation to the project ***[Part 10, Division 15, clause 242]***.

Unit entitlement

6.89 The unit entitlement for a reforestation reporting period to be specified in a certificate of reforestation be the lesser of ***[Part 10, Division 3, clause 196]***:

- the net total number of tonnes of greenhouse gases removed by the forest stand or stands in the project less the net total number of units issued in relation to the project; or

- the reforestation unit limit less the net total number of units issued in relation to the project.

6.90 The intention is that the calculation of the unit entitlement will be undertaken using information provided by the carbon sequestration right holder on:

- forest management actions (e.g. forest establishment date, species planted and any harvesting events)

- natural disturbances such as fire and wind-throw.

6.91 Scheme units will only be issued as net greenhouse gas removals occur, not in advance

Decision by a computer program

6.92 The Authority will have the capacity to make use of a computer program for the purpose of working out the unit entitlement to be specified in a certificate of reforestation ***[Part 10, Division 3, clauses 195, 196].***

6.93 It is envisaged that the computer program used for this purpose will incorporate an updated version of the National Carbon Accounting Toolbox.

6.94 It is intended that further provisions will be included in the bill to enable a carbon sequestration right holder to apply for modifications to be made to aspects of the parameter values underlying the computer program including in relation to calculation of a unit entitlement.

Variation and revocation of an eligible reforestation project

Voluntary variation

6.95 A carbon sequestration right holder in relation to an eligible reforestation project can apply to vary the boundaries of the area or areas of land involved in the project ***[Part 10, Division 5, clause 210].*** If accepted, such a variation would be effected by means of the variation of the declaration of the project as an eligible reforestation project.

6.96 It is intended that an application for a variation could be made at the same time as a reforestation report on the project is submitted.

6.97 An application must be in the approved form and must be accompanied by the information and documents (if any) specified in the regulations ***[Part 10, Division 5, clause 210].***

6.98 The criteria on which the Authority is to decide an application for variation of a project (set out in clause 212) are the same as those that apply where the Authority is considering whether to declare a reforestation project to be an 'eligible reforestation project' (see clause 209). The Authority cannot make the variation requested by the carbon sequestration right holder unless satisfied that the project (as varied) will meet those criteria ***[Part 10, Division 5, clause 212].***

6.99 An application for variation of a project can be withdrawn at any time before the Authority has made a decision on the application ***[Part 10, Division 5, clause 211].***

6.100 If an application is withdrawn, the Authority is required to refund any application fee paid by the applicant ***[Part 10, Division 5, clause 211].***

6.101 Withdrawal of an application does not prevent the applicant from making a fresh application for variation of the project boundaries ***[Part 10, Division 5, clause 211].***

6.102 The Authority must take all reasonable steps to ensure that a decision is made on an application for variation within 90 days of the application or, if the applicant was required to provide further information in connection with the application, receipt of that information.

6.103 A variation takes effect immediately after it is made. The Authority must give a copy of the variation to the applicant as soon as practicable after it is made.

6.104 If the Authority decides to refuse to make the requested variation, the applicant must be given written notice of this ***[Part 10, Division 5, clause 212].***

Unilateral variation

Clearing of part of a forest

6.105 In certain circumstances, the Authority will be required to vary the declaration of a project as an eligible reforestation project. Under clause 213, such a variation must be made if a part of the project area (or a project area) involved in the project has remained clear of an area of forest for a continuous period of 5 years ***[Part 10, Division 5, clause 213].***

6.106 In these circumstances, the Authority must, in writing, vary the declaration so as to exclude the area of land that has remained clear of a forest stand ***[Part 10, Division 5, clause 213].***

- This will reduce the scope for 'gaming' in relation to the unit limit for a project by means of the inclusion in the project of areas of land on which it is not in fact intended that a forest will be established.

Eligibility criteria not met

6.107 The Authority may unilaterally vary the declaration of a project as an eligible reforestation project if a part of the project area (or a project area) involved in the project ceases to meet one or more of the eligibility criteria relating to eligible reforestation projects ***[Part 10, Division 5, clause 214].***

- This could occur, for example, if it were determined that the vegetation established for the purposes of a reforestation project is comprised of species that do not have the potential to reach a height of at least 2 metres.

6.108 Before varying a declaration on this basis, the Authority must inform the carbon sequestration right holder of the proposed variation, and invite that person to make a submission about the proposal. If such a submission is made, the Authority must consider this in deciding whether to vary the declaration.

6.109 The carbon sequestration right holder in relation to a project will be notified as soon as practicable of any unilateral variation of the project made by the Authority ***[Part 10, Division 5, clauses 213, 214].***

Voluntary revocation

6.110 The person who holds the carbon sequestration right in relation to a reforestation project may apply to the Authority for the revocation of the declaration that declares the project to be an eligible reforestation project.

6.111 In effect, this provision allows a carbon sequestration right holder to 'opt out' of the reforestation scheme.

6.112 If an applicant for such a revocation has relinquished the net total number of units (if any) that have been issued in relation to the project, the Authority must revoke the declaration ***[Part 10, Division 5, clause 215, 216].***

6.113 An application must be in the approved form ***[Part 10, Division 5, clause 215, 216].***

6.114 As soon as practicable after revoking the declaration, the Authority will given the carbon sequestration right holder in relation to the project a copy of the revocation ***[Part 10, Division 5, clause 215, 216].***

Unilateral revocation

Forest cleared

6.115 If the whole of the project area (or areas) involved in a project has remained clear of an area of forest for a continuous period of at least 5 years, the Authority must revoke the declaration of the project as an eligible reforestation project ***[Part 10, Division 5, clause 217].***

- This could occur because, for example, the reforestation project was not undertaken, or the forests involved in the project are cleared and not re-established. If units have been issued in respect of the project, a relinquishment notice would be issued following such a revocation.

Eligibility criteria not met

6.116 The Authority may unilaterally revoke the declaration of a project as an eligible reforestation project if satisfied that the project does not satisfy one or more reforestation scheme eligibility requirements ***[Part 10, Division 5, clause 218].***

- This could occur where, for example, the forest involved in the project was harvested and subsequent re-establishment used a species that did not have the potential to reach a height of at least 2 metres, or establishment was not properly carried out and, as a result, the vegetation did not have the potential to attain a crown cover of at least 20 percent.

6.117 Before revoking a declaration on this basis, the Authority must inform the carbon sequestration right holder of the proposed revocation, and invite that person to make a submission about the proposal. If such a submission is made, the Authority must consider this in deciding whether to revoke the declaration.

Transfer of carbon sequestration right

6.118 The Authority must revoke the declaration of a project as an eligible reforestation project where the person who held the carbon sequestration right in relation to the project ceases to hold that right, and,

within 90 days of that occurrence, there was no 'relinquishment obligation transfer agreement' in force ***[Part 10, Division 5, clause 219].***

6.119 A person may cease to hold a carbon sequestration right for a number of reasons, for example:

- The carbon sequestration right has been sold to another person.
- The carbon sequestration right resulted from the person holding an interest in the relevant area of land - for example, a lease - for a fixed period of time, and that period has expired.
- The carbon sequestration right has passed to a beneficiary under a will.

6.120 If units have been issued in relation to an eligible reforestation project and the person who held the carbon sequestration right in relation to the project ceases to hold that right, the person must, within 90 days after the cessation occurs, notify the Authority ***[Part 10, Division 11, clause 235].***

6.121 Consideration is currently being given to how the relevant provisions in Part 10 of the draft bill should operate in a case where, upon the death of a carbon sequestration right holder, the right passes to another person as part of the deceased person's estate. Further provisions will be included in the bill to address this situation.

Relinquishment of Australian Emissions Units

Relinquishment – revocation of eligible project

6.122 The Authority will issue a notice of relinquishment to the holder of the carbon sequestration right in relation to a project if the declaration of the project as an eligible reforestation project has been revoked and units have been issued for the project ***[Part 10, Division 10, clause 232].***

6.123 The notice of relinquishment will be for the net total number of units issued in relation to the reforestation project.

6.124 The Authority must not issue such a notice if 130 years have passed since the first units were issued in relation to the project ***[Part 10, Division 10, clause 232].***

6.125 Chapter 9 of the commentary contains a detailed discussion of the penalties for failure to comply with a requirement to relinquish Australian emissions units.

Relinquishment – decrease in reforestation unit limit

6.126 The Authority will issue a notice of relinquishment to the holder of the carbon sequestration right in relation to an eligible reforestation project if there is a decrease in the unit limit for the project and the number of units that have already been issued exceeds this decreased number.

6.127 The notice must specify the number of units that must be relinquished, which will be the difference between the net total number of units issued and the new (lower) unit limit for the project.

6.128 The Authority must not issue such a notice if 130 years have passed since the first units were issued for the project ***[Part 10, Division 10, clause 233].***

6.129 Chapter 9 of the commentary contains a detailed discussion of the penalties for failure to comply with a requirement to relinquish Australian emissions units.

Relinquishment obligation transfer agreement

6.130 A relinquishment obligation transfer agreement is an agreement between a carbon sequestration right holder in relation to an eligible reforestation project and a person to whom that right is or has been transferred (the transferee) ***[Part 10, Division 10, clause 234].***

6.131 Clause 234(2) sets out the conditions that must be satisfied if an agreement is to constitute a 'relinquishment obligation transfer agreement', for the purposes of the draft bill. First, the transferee must be a recognised reforestation entity. Secondly, a relinquishment obligation transfer agreement must state that the transferee accepts responsibility for complying with any requirements to relinquish units that may in future be imposed on the transferee in relation to the project. Thirdly, the Authority must have given written approval of the agreement.

6.132 A further condition is that, if the Authority has required the transferee to give security to the Commonwealth in relation to the fulfilment by the transferee of any potential future requirement to relinquish units, the transferee must have given that security.

6.133 A relinquishment obligation transfer agreement remains in force until the transferee ceases to hold the carbon sequestration right in relation to the project to which the agreement relates ***[Part 10, Division 10, clause 234].***

Relinquishment - transfer of carbon sequestration right

6.134 The consequences that will follow from a person ceasing to hold the carbon sequestration right in relation to an eligible reforestation project (whether by voluntary transfer or otherwise) will depend on the circumstances in which this occurs. There are two possibilities:

- if a relinquishment obligation transfer agreement is in place, the transferee effectively takes the place of the original carbon sequestration right holder in relation to the eligible reforestation project in question; or

- if no such agreement is in place within 90 days of the original carbon sequestration right holder ceasing to hold that right, the Authority will unilaterally revoke the declaration of the project as an eligible reforestation project and issue to that person a notice requiring relinquishment of the net total number of units issued for the project (in accordance with clause 232).

6.135 A holder of the carbon sequestration right in relation to an eligible reforestation project may cease to hold that right in a variety of different circumstances:

Example 6.1 Transfer of a carbon sequestration right

Carbon Sinks Australia holds the carbon sequestration right in relation to an eligible reforestation project but no underlying estate or interest in the land. The company no longer wants to be involved in reforestation activities.

Another recognised reforestation entity, Forests Forever, is interested in expanding their carbon sink business.

Carbon Sinks Australia and Forests Forever enter into a relinquishment obligation transfer agreement and Forests Forever buys the carbon sequestration right from Carbon Sinks Australia.

Forests Forever becomes the new reforestation scheme participant with respect to the eligible reforestation project. From this point in time Forests Forever will be responsible for meeting scheme reporting requirements and any future relinquishment requirements in relation to the project. They will also be able to apply for and be issued with a certificate of reforestation, and be issued with units.

If Carbon Sinks Australia had been issued with a relinquishment notice before they sold the carbon property right, this notice and any administrative penalty payable for a failure to relinquish units, continues to apply to them and not to Forests Forever.

Example 6.2 Transfer of freehold land with reforestation project

Mr and Mrs MacDonald have a farm that includes an eligible reforestation project – consisting of fully grown trees planted along fence lines. They have received 10, 000 units for this project and will not receive further units because the trees are fully grown. They want to move to Queensland to be closer to family.

A neighbour is interested in buying the property. He doesn't have any plans to cut down the trees but recognises that he will have to relinquish units if he changes his mind and wants to remove the trees in future. For this reason, he is not willing to pay as much for the land as he would have done if it did not include the eligible reforestation project.

The MacDonalds and the neighbour agree to a reduced sale price that takes account of the potential obligation to relinquish units if the trees were subsequently removed.

Example 6.3 Cessation of a carbon sequestration right

Forests Forever has an eligible reforestation project - the Big Trees Project - in an area which, since the trees were established, has had below average rainfall. Forests Forever has received 20, 000 units in relation to the project but is concerned that the rate of return on the project will be lower than expected.

A developer is interested in buying the land to build a logistics depot. The developer offers Forests Forever a price for the land that is reduced to reflect the number of units they would have to relinquish when they remove the forest.

Forests Forever decide to have the declaration of the Big Trees project as an eligible reforestation project revoked and to meet the related relinquishment obligation themselves. The company has 5, 000 units which it has received in relation to other reforestation projects but has not yet sold. The company buys another 15, 000 units from the carbon market. It relinquishes the 20, 000 units that it has received in relation to the Big Trees Project. The declaration of that project as an eligible reforestation project would be revoked and no further Scheme obligations would apply.

The land is sold to the developer at a higher price than would have been paid if it was subject to potential Scheme obligations.

Forest maintenance obligation

6.136 In very limited circumstances, a person may become subject to a forest maintenance obligation in relation to an area of land that is or was a project area involved in an eligible reforestation project. The forest maintenance obligation can only take effect where a relinquishment notice is issued to the person who holds or held the carbon sequestration right in relation to the project but is not complied with within 90 days. The person who is required to satisfy the forest maintenance obligation is the person who, at any point in time while the obligation operates, holds the forestry right in relation to the land in question ***[Part 10, Division 9, clause 226]***. This may or may not be the same person who holds the carbon sequestration right in relation to the project.

6.137 At the time the forest maintenance obligation comes into operation, one or more forest stands may or may not be in existence on the land in question. Therefore, the obligation will require the holder of the forestry right either:

- where forest stands are in existence on the relevant land, to ensure that one or more of those stands are maintained such that it is reasonable to expect that, at maturity, the net number of tonnes of greenhouse gases removed by the stand or stands are equivalent to the net total number of units issued in relation to the project; or

- where no forest stand is in existence on the land, establish and maintain a forest stand or stands such that it is reasonable to expect that, at maturity, the net number of tonnes of greenhouse gases removed by the stand or stands are equivalent to the net total number of units issued in relation to the project ***[Part 10, Division 9, clause 226].***

6.138 The Authority will be able to use a computer program to determine whether forest stands established and maintained for the purposes of the forest maintenance obligation will achieve an amount of net greenhouse gas removals that is equivalent to the net total number of units that have been issued for the project ***[Part 10, Division 9, clause 226]***.

6.139 The forest maintenance obligation will cease when:

- the penalty payable under clause 287 of the draft bill in respect of the carbon sequestration right holder's failure to comply with the relinquishment notice is paid in full, including any late payment penalty; or

- the forestry right holder relinquishes the net total number of units issued in respect of the eligible reforestation project; or

- at the end of 130 years after the first occasion on which an Australian emissions unit was issued in relation to the project.

6.140 It should be noted that the cessation of the forest maintenance obligation will not mean that the forest can be dealt with contrary to any other obligations or requirements that may apply under other legislative regimes, such as, for example, State or Territory planning or vegetation-related laws.

Injunctions

6.141 The Authority may apply to the Federal Court for an injunction requiring a person to do or not do something to ensure the forest maintenance obligation is complied with ***[Part 10, Division 9, clause 227, 230, 231]***.

6.142 The Federal Court may grant an interim injunction before considering the application for an injunction ***[Part 10, Division 9, clause 228]***.

6.143 The Federal Court may discharge or vary any injunction granted with respect to a forest maintenance obligation ***[Part 10, Division 9, clause 229]***.

Register of Reforestation Projects

6.144 The Authority must keep a public, electronic register of reforestation projects ***[Part 10, Division 13, clause 238].***

6.145 The Register will contain information about eligible reforestation projects including :

- the project boundaries

- the name of the person who is the carbon sequestration right holder in relation to the project

- the unit limit for the project

- the number of units that have been issued in relation to the project and the person or persons to whom they have been issued

- the number of units (if any) that have been relinquished in connection with the project
- whether the land involved in the project is subject to a forest maintenance obligation
- such further information (if any) relating to the reforestation project as the Authority considers appropriate.

[Part 10, Division 13, clause 239]

6.146 The register will serve two purposes. The first is to provide information to prospective buyers of interests in the land on which an eligible reforestation project is being, or was, carried out about potential scheme benefits, as well any liabilities that have arisen in connection with the project. The second is to provide information to the market about the number of units likely to be issued in respect of net greenhouse gas removals resulting from eligible reforestation projects.

Entries in title registers

6.147 Clause 236 of the draft bill is concerned with the making of entries by State or Territory Registrars of Title (or similar) in land titles registers in relation to eligible reforestation projects that are, or were, carried out on areas of land included in those registers ***[Part 10, Division 12, clause 236]***.

6.148 Such entries will ensure that, if an area of land is the subject of an eligible reforestation project, prospective purchasers of interests in the land are made aware of that fact and can then ascertain what, if any, implications this may have under the reforestation scheme.

6.149 Clause 237 is specifically concerned with the making of entries in land titles registers to ensure that, where an area of land included in such a register is subject to a forest maintenance obligation under the reforestation scheme, prospective purchasers' attention is drawn to that fact ***[Part 10, Division 12, clause 237]***.

6.150 It is intended that the Authority will have administrative arrangements in place to ensure that State and Territory land titles officials receive timely notification of the declaration of eligible reforestation projects, variations and revocations of such declarations, and when land becomes subject to a forest maintenance obligation.

Transitional provisions

6.151 Forests have been part of other greenhouse gas abatement schemes such as the New South Wales and Australian Capital Territory Greenhouse Gas Reduction Scheme and the Australian Government's Greenhouse Friendly scheme.

6.152 These forests could be included in eligible reforestation projects under the reforestation scheme in Part 10 of the draft bill.

6.153 Consideration is being given to transitional provisions for these forests.

Chapter 7
Destruction of synthetic greenhouse gases

Outline of chapter

7.1 Part 11 of the draft bill provides for the issue of free Australian emissions units to entities that arrange for the destruction of synthetic greenhouse gases in accordance with scheme requirements.

7.2 Divisions 2 and 3 specify who is entitled to apply for a certificate of eligible synthetic greenhouse gas destruction, pursuant to which free Australian emissions units will be issued. Division 4 deals with the process of recognising a person as a synthetic greenhouse gas destruction customer – one type of entity eligible to apply for a certificate of eligible synthetic greenhouse gas destruction.

Context of new law

7.3 As outlined in Chapter 1, liability for synthetic greenhouse gas emissions is imposed on entities which import or manufacture synthetic greenhouse gases, based on the carbon dioxide equivalence of these gases. Applying liability in this way assumes that gases are emitted. However a portion of these gases may be recovered from the equipment in which they are employed, and may be destroyed in certain high temperature incineration devices.

7.4 Free Australian emissions units will be allocated to companies that destroy, or arrange for the destruction of, synthetic greenhouse gases in accordance with scheme verification requirements. This will provide an incentive for the recovery and disposal of these gases. It will also enable persons to recoup the cost of scheme liability imposed on gases that are subsequently recovered and destroyed. By increasing available abatement options, this will enable the Scheme cap to be achieved at a lower cost than would otherwise be possible.

Summary of new law

7.5 The Authority may, upon application by an eligible entity, issue a certificate of eligible synthetic greenhouse gas destruction. ***[Part 11, Division 3, clause 246]*** A certificate may be issued to a recognised synthetic greenhouse gas destruction customer or the operator of an approved synthetic greenhouse gas destruction facility and is issued, broadly, on the basis that the customer or facility has destroyed or arranged for the destruction of eligible synthetic greenhouse gases in accordance with scheme requirements.

7.6 The certificate must state that a specified number is the unit entitlement in respect of the certificate. ***[Part 11, Division 3, clause 249]*** The Authority must issue, to the holder of a certificate of eligible synthetic greenhouse gas destruction, a number of free Australian emissions units equal to the number specified in the certificate as the unit entitlement for that certificate. ***[Part 11, Division 2, clause 245]***

7.7 A simplified outline is included in Part 11. ***[Part 11, Division 1, clause 244]***

Detailed explanation of new law

Who is eligible to apply for a certificate of eligible synthetic greenhouse gas destruction

7.8 Only recognised customers of synthetic greenhouse gas destruction facilities and operators of an approved synthetic greenhouse gas destruction facility will be eligible to apply for a certificate of eligible synthetic greenhouse gas destruction, in respect of which free Australian emissions units may be issued. ***[Part 11, Division 3, clause 246]***

Approved customers of SGG destruction facilities

7.9 A company that is not an operator of an approved synthetic greenhouse gas destruction facility will need to be recognised as a synthetic greenhouse gas destruction customer before it is entitled to make an application for a certificate of eligible synthetic greenhouse gas destruction. A company must apply to the Authority to become a recognised synthetic greenhouse gas destruction customer. ***[Part 11, Division 4, clause 253]***

7.10 The regulations will specify information and documents (if any) that a person will be required to submit as part of an application. The

purpose of such information and documents is to enable the Authority to make a decision on an application. ***[Part 11, Division 4, clause 254]***

7.11 The Authority may, by written notice, require an applicant to provide additional information that the Authority considers necessary to make a decision on an application. In the event that information is not provided within the time frame stated on the notice, the Authority may refuse the application. ***[Part 11, Division 4, clause 255]***

7.12 The regulations may specify an application fee. The purpose of the fee is to enable the Authority to recover costs associated with processing the application. An application fee is considered appropriate given that participation in destruction under the scheme will be voluntary, open to any company, and will deliver financial benefits. Moreover, the Authority will incur costs in the process of conducting fit and proper person tests. ***[Part 11, Division 4, clause 254]***

7.13 The Authority may recognise a company as a synthetic greenhouse gas destruction customer if satisfied that the company is a fit and proper person. In making this assessment the Authority must have regard to matters that include any convictions against a law of the Commonwealth, State or Territory relating to dishonest conduct, breaches of this Act or the associated provisions, and whether the company is under external administration. The Authority may also consider such other matters (if any) that it considers relevant. ***[Part 11, Division 4, clause 256]***

7.14 The regulations may specify additional eligibility criteria, such as a requirement that the applicant have some other type of approval or licence under a Commonwealth, State or Territory law that is relevant to synthetic greenhouse gas destruction.

7.15 The application of a fit and proper person test seeks to minimise the risk of any fraudulent activity in relation to destruction of synthetic greenhouse gases under the scheme.

7.16 The Authority will have the power to cancel a company's recognition where the Authority is no longer satisfied that the company remains a fit and proper person having regard to the same criteria. ***[Part 11, Division 4, clause 257]***

7.17 A recognised synthetic greenhouse gas destruction customer may surrender the customer's recognition by written notice to the Authority. ***[Part 11, Division 4, clause 258]***

7.18 If a company is a recognised synthetic greenhouse gas destruction customer, the company's recognition is not transferable. ***[Part 11, Division 4, clause 259]***

Approved SGG destruction facilities

7.19 The term "approved synthetic greenhouse gas destruction facility" is defined by reference to the meaning it is proposed it be given in the *Ozone Protection and Synthetic Greenhouse Gas Management Regulations 1995.* ***[Part 1, clause 5, definition of 'approved synthetic greenhouse gas destruction facility']*** This definition anticipates amendments to the *Ozone Protection and Synthetic Greenhouse Gas Management Regulations 1995* that will provide for the approval of synthetic greenhouse gas destruction facilities.

7.20 It is anticipated that the approval process would build on existing processes in place to approve "refrigerant destruction facilities" and "extinguishing agent destruction facilities" and involve, amongst other things, the applicant:

- demonstrating that the facility can destroy one or more of the three classes of synthetic greenhouse gas - hydrofluorcarbons (HFCs), perfluorocarbons (PFCs) and sulphur hexafluoride (SF_6)

- passing a fit and proper person test similar to that required of recognised customers of synthetic greenhouse gas destruction facilities.

Application for certificate of eligible synthetic greenhouse gas destruction

7.21 Applications for a certificate of eligible synthetic greenhouse gas destruction can be made within 4 months of the end of a financial year. ***[Part 11, Division 3, clause 246]*** An application must be in an approved form and must be accompanied by such information and documents (if any) as specified in the regulations. ***[Part 11, Division 3, clause 247]***

7.22 The Authority may, by written notice require an applicant to give further information in respect of an application. If the applicant fails to provide the required information within the period specified in the notice the Authority may refuse to consider the application or refuse to take any action, or any further action in relation to the application. ***[Part 11, Division 3, clause 248]***

7.23 An application must specify one or more synthetic greenhouse gas destruction events. ***[Part 11, Division 3, clause 246]***

7.24 A synthetic greenhouse gas destruction event means an event that consists of the destruction of a particular quantity of a particular kind

of synthetic greenhouse gas. ***[Part 1, clause 5, definition of 'synthetic greenhouse gas destruction event']***

7.25 An application may be made by a person in the person's capacity as an approved synthetic greenhouse gas destruction facility, or a recognised customer of a synthetic greenhouse gas destruction facility, but not both. ***[Part 11, Division 3, clause 246]***

7.26 Allowing approved synthetic greenhouse gas destruction facilities, or recognised customers of synthetic greenhouse gas destruction facilities, to apply for a certificate of eligible synthetic greenhouse gas destruction will increase opportunities for this form of abatement. This also enables destruction facilities and their customers to determine the most efficient option for submitting applications for synthetic greenhouse gas destruction.

Issue of certificate to recognised synthetic greenhouse gas destruction customer

7.27 The Authority may issue a certificate to a recognised synthetic greenhouse gas destruction customer who makes an application in that capacity where:

- the Authority is satisfied that the following conditions are met in relation to each synthetic greenhouse gas destruction event specified in the application:
  - the event occurred during the relevant financial year
  - the applicant was a recognised synthetic greenhouse gas destruction customer at the time the event occurred
  - the synthetic greenhouse gas was destroyed at an approved synthetic greenhouse gas destruction facility under a contract between the applicant and the operator of the facility
  - the applicant incurred expenditure under the contract in respect of the destruction
  - the approved synthetic greenhouse gas destruction facility was authorised under the *Ozone Protection and Synthetic Greenhouse Gas Management Regulations 1995* to carry out the destruction of the synthetic greenhouse gas
  - the destruction complied with the *Ozone Protection and Synthetic Greenhouse Gas Management Regulations 1995*

– the gas was eligible waste.

- the total quantity of synthetic greenhouse gas destroyed exceeds the quantity specified in the regulations.

[Part 11, Division 3, clause 250 (2)]

Issue of certificate to operator of an approved synthetic greenhouse gas destruction facility

7.28 The Authority may issue a certificate to the operator of an approved synthetic greenhouse gas destruction facility who applies in that capacity, where:

- the Authority is satisfied that the following conditions are met in relation to each synthetic greenhouse gas destruction event specified in the application:

  – the event occurred during the relevant financial year

  – the synthetic greenhouse gas was destroyed at an approved synthetic greenhouse gas destruction facility operated by the applicant

  – the destruction of the synthetic greenhouse gas was not carried out under a contract between the applicant and another person

  – the applicant was not entitled to receive any consideration for carrying out the destruction of the synthetic greenhouse gas

  – the approved synthetic greenhouse gas destruction facility was authorised under the *Ozone Protection and Synthetic Greenhouse Gas Management Regulations 1995* to carry out the destruction of the synthetic greenhouse gas

  – the destruction complied with the *Ozone Protection and Synthetic Greenhouse Gas Management Regulations 1995*

  – the gas was eligible waste.

- the total quantity of synthetic greenhouse gas destroyed exceeds the quantity specified in the regulations.

[Part 11, Division 3, clause 250(3)]

7.29 A test based on entitlement to receive consideration under a contract is used to distinguish between:

- when a destruction facility contracts a recognised customer to supply the destruction facility with waste synthetic greenhouse gas that the destruction facility subsequently destroys, and
- when a recognised customer contracts a destruction facility to provide a destruction service.

[Part 11, Division 3, clause 250(2)] [Part 11, Division 3, clause 250(3)]

7.30 The purpose of placing a threshold on the amount of synthetic greenhouse gas destroyed is to ensure that the Authority is not burdened by a large number of applications for small destruction events or a large number of applications from small operations. This will also increase the efficiency of synthetic greenhouse gas destruction.

Destruction of synthetic greenhouse gases in accordance with the Ozone Protection and Synthetic Greenhouse Gas Management Regulations 1995

7.31 It is anticipated that amendments to the *Ozone Protection and Synthetic Greenhouse Gas Management Regulations 1995* will require destruction facilities, when operating as approved synthetic greenhouse gas destruction facilities, to destroy synthetic greenhouse gases in accordance with certain verification requirements. These will be designed to enable verification of quantities and kinds of synthetic greenhouse gases destroyed during synthetic greenhouse gas destruction events.

Eligible waste

7.32 Regulations will be made to define the types of waste that will be eligible under the Scheme. The intent of these regulations is to ensure that there are no perverse incentives to stockpile synthetic greenhouse gases prior to Scheme commencement for the purpose of destroying them to gain Australian emissions units.

Issue of certificate of eligible synthetic greenhouse gas destruction

7.33 If the Authority is satisfied that a recognised synthetic greenhouse gas destruction customer or operator of an approved synthetic greenhouse gas destruction facility meets the relevant eligibility criteria, and the amount of gas specified in the application exceeds a threshold specified in the regulations, the Authority may issue a certificate of eligible synthetic greenhouse gas destruction. ***[Part 11, Division 3, clause 250]***

7.34 The issue of a certificate of eligible synthetic greenhouse gas destruction entitles the holder of a certificate to a unit entitlement - a specified number of free Australian emissions units. ***[Part 11, Division 3, clause 249]***

7.35 A certificate of eligible synthetic greenhouse gas destruction is not transferable. ***[Part 11, Division 3, clause 252]***

7.36 As soon as practicable after the day on which a certificate of eligible synthetic greenhouse gas destruction was issued the Authority must issue a number of free Australian emissions units equal to the number specified in the certificate as the unit entitlement for that certificate***. [Part 11, Division 2, clause 245]***

7.37 The unit entitlement will be determined by calculating a provisional number for each synthetic greenhouse gas event to which the certificate relates and adding together those provisional numbers. Each provisional number will be calculated by multiplying the amount of synthetic greenhouse gas submitted for destruction in the destruction equipment (in tonnes of carbon dioxide equivalence) by a destruction/removal efficiency factor for the approved destruction facility at which the event took place. ***[Part 11, Division 3, clause 251]***

7.38 The application of a destruction/removal efficiency factor recognises that the efficiency of destruction may vary for different types of destruction equipment and different classes of synthetic greenhouse gases.

Chapter 8
Assessment, surrender, relinquishment and voluntary cancellation

Outline of chapter

8.1 This chapter describes how liability is calculated, advisory assessments of an entity's emissions number, the obligation to surrender and shortfalls. It also describes the surrender, relinquishment and voluntary cancellation mechanisms.

8.2 It relates to Parts 5, 6, 14 and 15 of the draft bill.

Context

8.3 The Carbon Pollution Reduction Scheme imposes obligations on liable entities in relation to the emissions or potential emissions for which they are responsible. Details of these concepts are provided in Chapter 1 of this commentary.

8.4 Liable entities will be required to report emissions or potential emissions under the *National Greenhouse and Energy Reporting Act 2007*, which is to be amended. The proposed amendments to that Act are described in a separate commentary on the proposed Carbon Pollution Reduction Scheme (Consequential Amendments) Bill 2009 (the draft consequential amendments bill).

8.5 This chapter focuses on the mechanisms within the draft Carbon Pollution Reduction Scheme Bill for assessment and surrender of eligible emissions units. It also addresses the mechanisms for:

- relinquishment of units by, for example, the recipient of units under the emissions-intensive trade-exposed assistance program
- voluntary cancellation of units.

Summary

The emissions number

8.6 A liable entity is required to surrender one eligible emissions unit for each tonne of emissions for which the entity is responsible. The total quantity of emissions for which the entity is responsible is known as the 'emissions number'. This number is calculated using the following formula:

> Entity's emissions number = the sum of its provisional emissions numbers - the excess surrender number + the make good number.

8.7 Each of these concepts is explored in the Detailed Explanation section below.

8.8 Part 5 of the draft bill relates to emissions numbers. It includes a simplified outline ***[Part 5, clause 124].***

Assessments

8.9 The Scheme is based on a self-assessment approach where liable entities calculate their own emissions numbers and report them under the *National Greenhouse and Energy Reporting Act 2007*, which will be amended.

8.10 The Authority may issue assessments of the emissions number to a liable entity if no report of its greenhouse gas emissions was lodged in accordance with the requirement in the *National Greenhouse and Energy Reporting Act 2007* or if the Authority has reasonable grounds to believe that the emissions number specified in the report is incorrect.

8.11 These assessments are advisory in nature. An assessment does not make an entity liable. Liability arises from, for example, the emission of greenhouse gas from the operation of a facility, and does not necessarily involve assessment by the Authority.

Surrender

8.12 Each liable entity is required to surrender sufficient eligible emissions units to meet its obligation for a financial year, by 15 December of the following financial year.

8.13 An entity has a shortfall if it has not surrendered sufficient eligible emissions units to meet its obligation by 15 December.

8.14 The penalty for a shortfall is a monetary penalty and a 'make good' requirement. The monetary penalty is due and payable on 31 January in the following year. It is an administrative penalty. If it is not paid by that date, a late payment penalty applies and the Authority may take action to recover the debt. These and other penalties are addressed in Chapter 9 of this commentary.

8.15 The Authority is empowered to make an assessment of unit shortfall.

8.16 Part 6 of the draft bill relates to surrender. It includes a simplified outline ***[Part 6, Division 1, clause 128].***

Relinquishment

8.17 The process for relinquishment is separate but comparable to that for surrender. Persons will be required to relinquish units in the following situations:

- in the emissions-intensive trade-exposed assistance program, where, for example, planned production ceases during a year
- various situations where Australian emissions units have been issued in connection with reforestation – for example, where the person ceases to hold the carbon sequestration right in relation to a reforestation project and a relinquishment obligation transfer agreement was not in force
- where a court has ordered relinquishment following conviction under specified provisions of the Criminal Code relating to fraudulent conduct, including those relating to false or misleading statements in applications under the Scheme.

8.18 The situations in which a person is required to relinquish units are described in Chapter 4, 6 and 9 of this commentary. This chapter addresses the mechanism and the consequences of non-compliance, which are provided by Part 15 of the draft bill. Part 15 includes a simplified outline ***[Part 15, Division 1, clause 285].***

Voluntary cancellation

8.19 A registered holder of Australian emissions units, Kyoto units or non-Kyoto international emissions units may request the Authority to cancel one or more of those units. The mechanism is included in Part 14

of the draft bill and is described in this chapter. Part 14 includes a simplified outline ***[Part 14, clause 281].***

Detailed explanation of new law

Emissions number

8.20 Liability will be based on the emissions number which liable entities must include in their report to the Authority, in accordance with proposed amendments to the *National Greenhouse and Energy Reporting Act 2007* (See the draft consequential amendments bill, Schedule 1, Part 2, Item 181).

8.21 The emissions number is calculated using the following formula ***[Part 5, clause 125]***:

> Entity's emissions number = the sum of its provisional emissions numbers - the excess surrender number + the make good number

8.22 The following paragraphs describe the concepts which make up this formula: the provisional emissions number, excess surrender number and make good number.

8.23 A provisional emissions number represents the emissions which give rise to liability under the Scheme. Part 3 of the draft bill describes the situations which result in a provisional emissions number. These include the emission of greenhouse gases from facilities by direct emitters or holders of liability transfer certificates relating to such facilities (Part 3, Division 2); the import, manufacture and supply of synthetic greenhouse gas (Part 3, Division 3); the supply or use of eligible upstream fuel (Part 3, Division 4); and the receipt of eligible upstream fuels by persons quoting an OTN (Part 3, Division 4).

8.24 An excess surrender number can arise because the liable entity surrendered an excess number of emissions units for the previous financial year ***[Part 6, Division 4, clause 143(1)]***.

8.25 An excess surrender number cannot arise from excess surrender of units with the following year's vintage ('borrowing'). An entity can only surrender borrowed units during a limited period when its emissions number is known ***[Part 6, Division 2, clause 129(5)]***. An entity can only surrender the number of borrowed units up to 5% of its emissions number ***[Part 6, Division 4, clause 143(2)]***.

8.26 The make-good number reflects the unit shortfall of the liable entity for the previous financial year ***[Part 6, Division 4, clause 142(1)].***

8.27 The purpose of including a 'make good' requirement is to ensure that liable entities are required to surrender eligible emissions units to meet their obligations, not simply pay a financial penalty. It thus emphasises the environmental integrity of the scheme.

8.28 In cases where liability is transferred from a controlling corporation to a member of its group (through the issue of a liability transfer certificate by the Authority) and the group member which holds the certificate incurs a unit shortfall, then that shortfall is reflected in the make-good number of the controlling corporation rather than that of the member of the group ***[Part 6, Division 4, clause 142(2)].***

Example 8.1 Calculation of emissions number

In 2014-15, Company A is a controlling corporation of a group that contains two other entities B and C.

Company B has operational control of a facility that emits less than 25,000 tonnes of carbon dioxide equivalence and is therefore exempt from the scheme.

Company C has operational control of a facility that emits 530,000 tonnes.

Company A's provisional emissions number is therefore 530,000.

In the previous financial year (2013-14), Company A surrendered insufficient units and incurred a shortfall of 5,000 units. Company A therefore has a make good number of 5,000.

Company A's emissions number is 530,000 + 5,000 = 535,000.

Example 8.2

Entity Y imports synthetic greenhouse gases with a carbon dioxide equivalence of 50,000 tonnes, and operates a gas storage facility that does not emit any emissions other than synthetic greenhouse gases. Its provisional emissions number is therefore 50,000.

It has an excess surrender number of 20,000.

Entity Y's emissions number is 50,000 - 20,000 = 30,000

Assessment

8.29 There are two circumstances in which the Authority may make an assessment of the person's emissions number for a financial year and provide the person with written notice of it:

- when a liable entity has provided a report under section 22A of the *National Greenhouse and Energy Reporting Act 2007* (see the draft consequential amendments bill, Schedule 1, Part 2, Item 181) by 31 October but the Authority has reasonable grounds to believe that the number specified in the report as the person's emissions number is incorrect ***[Part 5, clause 126]***

- where no such report has been provided by 31 October and the Authority has reasonable grounds to believe that the person is a liable entity for the financial year ***[Part 5, clause 127].***

8.30 In both cases the assessment must be accompanied by a statement setting out the effect of clause 132 (the obligation to surrender sufficient emissions units) ***[Part 5, clauses 126(3) and 127(3)].***

8.31 Each of these assessments may be amended by the Authority at any time. If this is done, then written notice of it must be provided ***[Part 5, clauses 126(4), 126(5), 127(4), 127(5)].***

8.32 The original and any amended assessments are advisory in nature ***[Part 5, clauses 126(7) and 127(7)].*** This underlines that the obligation to surrender eligible emissions units stems from the emissions number, not from any action taken by the Authority.

Surrender

The obligation to surrender

8.33 When a liable entity has an emissions number for the financial year of 1 or more (and there is a national scheme cap in place), then the person must surrender sufficient units by 15 December in the following financial year to ensure that it does not have a unit shortfall ***[Part 6, Division 4, clause 132].***

What is a unit shortfall

8.34 If a liable entity has surrendered no eligible emissions units by 15 December, then its unit shortfall ***[Part 6, Division 3, clause 130]*** is the same as its emissions number ***[Part 6, Division 3, clause 130(2)].*** Similarly, if the

liable entity has surrendered some eligible emissions units in the period ending 15 December, then the unit shortfall is its emissions number less the number of surrendered units ***[Part 6, Division 3, clause 130(3)].***

8.35 If surrendered Australian emissions units representing more than 5% of the emissions number are 'borrowed' (that is, their vintage year follows the relevant financial year to which the surrender relates), then the excess number of units over the 5% are not regarded as surrendered for the relevant financial year ***[Part 6, Division 3, clause 130(4)]***.

Example 8.3 – Calculation of shortfall

On 31 October 2018, a liable entity submits its report under the *National Greenhouse and Energy Reporting Act 2007* for the financial year 2017-18. The report indicates that the entity's emissions number is 100,000. On 15 December 2018, the liable entity transmits a notice to the Authority specifying the surrender of the following units for the financial year 2017-18:

Vintage of units	***Number of units***
2015-16	10,000
2016-17	10,000
2017-18	70,000
2018-19	10,000
Total	100,000

The surrender of units with vintages belonging to the current year and previous financial years will be accepted. However, only 5% of 100,000 units, or 5,000 units, with a 2018-19 vintage may be surrendered for the year 2017-18. The liable entity will therefore have a unit shortfall of 5,000 for the financial year 2017-18.

Which units are eligible emissions units

8.36 Only 'eligible emissions units' can be used for surrender. This phrase is defined to mean Australian emissions units and eligible international emissions units ***[Part 1, clause 5, definition of 'eligible emissions unit'].***

8.37 Australian emissions units of the current or earlier vintage years may be surrendered ***[Part 6, Division 2, clause 129(4)].*** This in effect allows for 'banking' of units.

8.38 As indicated above, there is a limit on the number of 'borrowed' units (that is, units of the next vintage year) which can be used for surrender ***[Part 6, Division 3, clause 130(4)]***. In addition, 'borrowed' units can

only be surrendered within a specified period when the entity's emissions number is known ***[Part 6, Division 2, clause 129(5)]***.

8.39 A unit is an eligible international emissions unit ***[Part 1, clause 5, definition of 'eligible international emissions unit']*** if it is:

- a certified emission reduction other than a temporary certified emission reduction or a long-term certified emission reduction
- an emission reduction unit
- a removal unit
- a prescribed unit issued in accordance with the Kyoto rules
- a non-Kyoto international emissions unit.

8.40 Certified emission reductions, emission reduction units, and removal units are specific types of units established under the Kyoto Protocol. An explanation of the reasons for framing this definition in this way is included in Chapter 2 of this commentary.

8.41 Kyoto units must not be surrendered if the surrender would breach regulations made for the purpose of clause 113 (carry-over restrictions) ***[Part 6, Division 2, clause 129(6)]***. The carry-over restrictions are explained in Chapter 2 of this commentary.

8.42 Regulations may specify that an eligible international emission unit must not be surrendered in relation to a particular year ***[Part 6, Division 2, clause 129(7)].*** Including this provision is consistent with the policy that a type of eligible international emission unit can be disallowed for surrender at any time to ensure the environmental integrity of the Scheme and consistency with Australia's international objectives. However, the regulation-making power is restricted in that it cannot specify a past year or the current year.

8.43 In addition:

- Certain removal and emission reduction units may only be surrendered in relation to the first three years of the Scheme ***[Part 6, Division 2, clause 129(8)].***
- A non-Kyoto international emissions unit must not be surrendered if this would breach the surrender restrictions ***[Part 6, Division 2, clause 129(9)].***

How are eligible emissions units surrendered

8.44 A person may surrender eligible emissions units by electronic notice transmitted to the Authority ***[Part 6, Division 2, clause 129(1)].***

8.45 What constitutes an 'electronic notice transmitted to the Authority' is described in clause 8 of the draft bill. This allows the Authority to require the use of particular information technology requirements ***[Part 1, clause 8].***

8.46 The notice must specify the eligible emissions units being surrendered, the financial year to which the surrender relates and the person's relevant account number ***[Part 6, Division 2, clause 129(2)].***

What happens when a unit is surrendered

8.47 When an Australian emissions unit is surrendered, it is cancelled and the Authority must remove the entry for the unit from the Registry account of the person who has surrendered it ***[Part 6, Division 2, clause 129(10)].***

8.48 However, different processes are required in relation to eligible international emissions units. When an eligible international emissions unit is surrendered, the Authority must remove the unit from the Registry account of the person who has surrendered it. In addition:

- If the unit is a Kyoto unit, the Authority must make an entry for the unit in a Commonwealth holding account ***[Part 6, Division 2, clause 129(11)].*** This enables the Commonwealth to use the Kyoto unit to meet Australia's emissions reduction target under the Kyoto Protocol.

- If a non-Kyoto international emissions unit is surrendered, then the action required of the Authority will be specified in the regulations ***[Part 6, Division 2, clause 129(12)].***

8.49 It is necessary to provide that this action will be specified in the regulations because the concept of a 'non-Kyoto international emissions unit' provides for units issued under future international agreements and units issued outside Australia under a law of a foreign country ***[Part 1, clause 5, definition of 'non-Kyoto international emissions unit']***. It therefore seeks to provide for future recognition of new and additional units without amending the Act.

Assessment of unit shortfall

8.50 The Authority is empowered to make an assessment of a person's unit shortfall and give notice of this to the person ***[Part 6, Division 3, clause 131].***

8.51 The Authority can do this at any time if it had reasonable grounds to believe that the person had made a false or misleading statement to the Authority which is relevant to ascertaining the person's unit shortfall that year, or otherwise engaged in relevant fraudulent conduct ***[Part 6, Division 3, clause 131(2)].***

8.52 In other circumstances the Authority can only make such an assessment during the four years after the relevant financial year ***[Part 6, Division 3, clause 131(3)].*** This period is broadly consistent with amendment periods under current business tax provisions for entities with complex affairs.

8.53 The Authority can amend such assessments ***[Part 6, Division 3, clause 131(5) and (6)].*** It can also rely on a report provided by the person under proposed section 22A of the *National Greenhouse and Energy Reporting Act 2007* in making an assessment ***[Part 6, Division 3, clause 131(4)]***.

8.54 A notice of assessment of unit shortfall is prima facie evidence of matters set out in the notice in proceedings for recovery of an administrative penalty and late payment penalty ***[Part 6, Division 4, clause 140].***

What happens if there is a unit shortfall

8.55 If a person has a shortfall as at 15 December following the relevant financial year, then the person will have a make-good number ***[Part 6, Division 4, clause 142]*** which is discussed above, and is liable to pay an administrative penalty ***[Part 6, Division 4, clause 133]***. The administrative penalty is worked out using the formula:

> [Number of units in the unit shortfall] x [prescribed amount for the current financial year].

8.56 The amount mentioned in the second part of the formula is expected to be specified in regulations. The maximum prescribed amount (and the default amount if not regulations are made) is 110% of the 'benchmark average auction price' ***[Part 6, Division 4, clause 133].***

8.57 The 'benchmark average auction price' for a particular financial year is the greater of: the average auction price of units issued as the result of auctions at all auctions in the financial year or the average auction price of units issued at the last auction conducted in the financial year ***[Part 6,***

Division 4, clause 141]. It must be calculated and published by the Authority as soon as practicable after the end of each financial year ***[Part 6, Division 4, clause 133(3)].***

8.58 The administrative penalty becomes due and payable on 31 January following the relevant financial year ***[Part 6, Division 4, clause 134].***

8.59 From this time, a late payment penalty will accrue at a rate of 20% per annum (or a lower rate if prescribed in regulations). The Authority may remit the late payment penalty in whole or part ***[Part 6, Division 4, clause 135].***

8.60 The administrative penalty and the late payment penalty are a debt due to the Commonwealth which can be recovered by the Authority in a court with the relevant jurisdiction ***[Part 6, Division 4, clause 136].***

8.61 Amounts of a kind specified in regulations and due from the Commonwealth may be set off against the amount due to the Commonwealth in respect of the administrative or late payment penalty ***[Part 6, Division 4, clause 137].***

8.62 Overpayments of the administrative penalty or late payment penalty can be refunded ***[Part 6, Division 4, clause 139].***

8.63 Where liability has been transferred to another member of a corporate group under a liability transfer certificate, the controlling corporation which consented to the transfer is taken to have guaranteed the payment of the administrative and late payment penalty ***[Part 6, Division 4, clause 138].***

Relinquishment

When is relinquishment required

8.64 The situations in which relinquishment of Australian emissions units can be required are discussed in other parts of this commentary. In brief, persons will be required to relinquish units in the following situations:

- in the emissions-intensive trade-exposed assistance program, where, for example, units are provided at or before the beginning of each financial year but planned production ceases during a year. Relinquishment is required to prevent both windfall gains from units associated with production that does not take place and reductions in the supply of units that would otherwise be available for auction.

- various situations where Australian emissions units have been issued in connection with reforestation – for example, where an area of land that was the subject of a reforestation project has remained clear of a forest stand for a period of at least 5 years

- where a court has ordered relinquishment following conviction under specified provisions of the Criminal Code, including those relating to false or misleading statements in an application under the Scheme. In this case, relinquishment is required because the units would not have been issued if fraudulent conduct had not occurred.

How are Australian emissions units relinquished

8.65 A person who holds Australian emissions units can relinquish them by electronic notice transmitted to the Authority. The notice must specify, among other things, the reason for relinquishment ***[Part 15, Division 2, clauses 286(1) and (2)].***

What happens to relinquished units

8.66 Those units relinquished in connection with reforestation or destruction of synthetic greenhouse gases are cancelled and the Authority removes the entry from the person's registry account ***[Part 15, Division 2, clauses 286(3) and (6)].***

8.67 If the relinquishment is not connected with these provisions, then the Authority must transfer the relevant units to the Commonwealth relinquished units account and property in the unit is transferred to the Commonwealth ***[Part 15, Division 2, clauses 286(4) and (5)].*** These are then auctioned ***[Part 4, Division 2, clause 100].***

8.68 This approach has been taken because units issued in relation to reforestation and destruction of greenhouse gases are not within the scheme cap: cancellation ensures that the scheme cap is not artificially inflated.

8.69 The auction process is described in Chapter 3 of this commentary.

Failure to comply with relinquishment requirements

8.70 The consequences of a failure to comply with a relinquishment requirement are comparable to the consequences of a unit shortfall described above ***[Part 15, Division 3, clauses 287-291].***

8.71 The significant differences are:

- There is no 'make good' requirement
- The maximum and default amount of the administrative penalty is 200% of the benchmark average auction price ***[Part 15, Division 3, clause 287(2)].***

8.72 The reason for this approach is that the entity may no longer be in the business nor be liable in the future.

Voluntary cancellation

8.73 The draft bill provides for the voluntary cancellation of Australian emissions units, Kyoto units and non-Kyoto international emissions units ***[Part 14, clauses 282, 283 and 284].*** This implements the Government's policy that voluntary cancellation allows individuals and organisations to contribute to stronger national climate change mitigation, regardless of whether they have obligations under the Scheme, by reducing the supply of eligible emissions units.

8.74 In each case, the registered holder of the emissions units transmits an electronic notice to the Authority requesting the Authority to cancel the units. The notice must specify the units to be cancelled and the person's relevant accounts.

8.75 The action to be taken by the Authority varies depending on the type of unit.

8.76 If the request relates to an Australian emissions unit, then the unit is cancelled and removed from the person's registry account, and the Minister must direct the Authority to transfer a Kyoto unit from the Commonwealth holding account to a voluntary cancellation account before the end of the 'true-up period' for the relevant Kyoto commitment period ***[Part 14, clause 282(3)].*** This implements the Government's policy which recognises that in order for the voluntary cancellation of an Australian emissions unit to lead to additional global abatement a Kyoto unit needs to be voluntarily cancelled within the relevant commitment period.

8.77 If the request relates to a Kyoto unit, and if the Authority is satisfied that the transfer would not breach the regulations made for the purposes of implementing the Kyoto rules or the regulations made to comply with the commitment period reserve, then it must transfer the unit to a voluntary cancellation account ***[Part 14, clause 283(3)]***. Again, this implements the Government's policy on voluntary cancellation and allows private entities to cancel Kyoto units, which means they cannot be used by

Australia or another Kyoto Party for the purposes of meeting their emission reduction targets and therefore leads to additional global abatement.

8.78 If the request relates to a non-Kyoto international emissions unit, further action by the Authority is dependent on the regulations ***[Part 14, clause 284]***. The draft bill provides for the voluntary cancellation of non-Kyoto units but the detailed arrangements will be specified in regulations which would not be made until an international unit has actually been prescribed as a non-Kyoto international emissions unit. Chapter 2 discusses arrangements for non-Kyoto international emissions units more generally.

Chapter 9
Compliance and enforcement

Outline of chapter

9.1 This Chapter addresses the various mechanisms provided in the draft bill which relate to compliance and enforcement. These include information gathering, record keeping, monitoring, liability of company officers, administrative penalties and the make good requirement, criminal and civil penalties, enforceable undertakings and the anti-avoidance provisions.

9.2 The relevant provisions are in Parts 13, and 17 to 23 of the draft bill. The provisions relating to avoidance of thresholds are clauses 23 and 30. The provisions relating to the administrative penalty and make good requirement are in Parts 6 and 15.

Context

9.3 The Authority is responsible for ensuring compliance with the Scheme. Effective enforcement arrangements are vital to achieving the objectives of the Scheme. Non-compliance with obligations could bring the Scheme into disrepute and undermine its environmental integrity. Appropriate compliance and enforcement mechanisms are therefore essential.

Summary

9.4 The draft bill provides a series of mechanisms needed to ensure compliance and for enforcement.

9.5 They are listed below with references to the simplified outlines or provisions:

- Information-gathering powers ***[Part 17, clause 295]***
- Requirements to keep records ***[Part 18, clause 301]***
- Monitoring powers ***[Part 19, Division 1, clause 305]***

- Provisions relating to liability of officers of bodies corporate ***[Part 20, clause 323]***
- Administrative penalties and the make good requirement ***[Part 6, Division 4, clauses 133 and 142] [Part 15, Division 3, clause 287]***
- Civil penalties ***[Part 21, clause 326]***
- Various criminal penalties including offences relating to administrative penalties and fraudulent conduct ***[Part 13, clause 279] [Part 22, clause 339]***
- Enforceable undertakings ***[Part 23, clause 342]***
- Anti-avoidance provisions ***[Part 3, Division 2, clause 23] [Part 3, Division 3, clause 30].***

9.6 The possibility of a court order to relinquish units following conviction for various offences under the Criminal Code connected with the Scheme can also be seen as an enforcement mechanism. The relinquishment mechanism is addressed in Chapter 8 of this commentary, as are the situations in which relinquishment can be ordered.

9.7 The other mechanisms referred to above, for example information gathering and monitoring, are standard for a regulator with functions comparable to those which the Authority will have.

Detailed explanation of new law

Information-gathering powers

9.8 If the Authority believes on reasonable grounds that a person has information or a document that is relevant to the operation of the Act or associated provisions, the Authority will be empowered to require, by written notice, that person to give information or documents, or to provide copies ***[Part 17, clause 296].***

9.9 The phrase 'associated provisions' is defined to include the proposed Carbon Pollution Reduction Scheme Regulations, the provisions in the *National Greenhouse and Energy Reporting Act 2007* relating to reporting by liable entities, and specified provisions of the Criminal Code in so far as those sections relate to the Scheme ***[Part 1, clause 5, definition of 'associated provisions'].***

9.10 The written notice must provide at least 14 days' notice ***[Part 17, clause 296(3)].***

9.11 This is a civil penalty provision, as are the ancillary contraventions. General provisions relating to civil penalties, including the pecuniary penalties are included in Part 21 of the draft bill.

9.12 Inspection, copying and retention of documents produced to the Authority are addressed ***[Part 17, clause 298].*** Compensation for a requirement to provide copies is also addressed ***[Part 17, clause 297].***

9.13 The Authority may retain possession of documents produced for as long as is necessary. However, provision is made for supply of a certified copy to the person otherwise entitled to possession ***[Part 17, clause 299].***

9.14 A person is not excused from giving information or producing a document following notice from the Authority on the ground that it might incriminate them or expose them to a penalty. However, the information given or document produced, the giving of the information or document and any information, document, or thing obtained as a consequence is not admissible in evidence against an individual in specified circumstances:

- civil proceedings for the recovery of other than administrative penalties and late payment penalties in respect of failure to surrender or relinquish units

- criminal proceedings, unless the proceedings are for an offence that relates to information-gathering by the Authority, involving the provision of false or misleading information or documents.

[Part 17, clause 300].

Record-keeping requirements

9.15 Records will need to be kept by various Scheme participants to support the information which they provide under the Scheme. This will enable the Authority and, where relevant, inspectors and auditors, to check the accuracy and completeness of information provided to the Authority, for example information provided in applications leading to the administrative allocation of Australian emissions units.

9.16 The capacity to audit emissions data is essential to monitoring compliance and ensuring the integrity of the Scheme. Record keeping obligations already apply to reports under the *National Greenhouse and Energy Reporting Act 2007*. These obligations will be expanded by proposed amendments included in the draft consequential amendments bill.

9.17 The detailed record-keeping obligations where the information is relevant to the Carbon Pollution Reduction Scheme Bill will be specified in the regulations ***[Part 18, clause 302].***

9.18 Record-keeping obligations will also be imposed on:

- suppliers where a recipient quotes its OTN in relation to the supply ***[Part 18, clause 303]***
- suppliers where the recipient has quoted its OTN but the supplier has rejected the quotation ***[Part 18, clause 304].***

9.19 These provisions will require the records to be kept for five years and are civil penalty provisions. This period is consistent with obligations under the taxation system.

9.20 These requirements and the ancillary contraventions are civil penalty provisions ***[Part 18, clauses 302-304].***

Monitoring powers

Introduction

9.21 In brief, Part 19 provides for the appointment of inspectors who may enter premises for the purpose of determining whether the Act or associated provisions have been complied with or substantiating information provided under the Act or associated provisions. The most usual duties of an inspector are expected to be examining documentation, for example records held by liable entities and operators of facilities covered by the Scheme. Entry must be with the consent of the occupier of the premises or under a monitoring warrant. An inspector who enters premises may exercise monitoring powers. He or she may be assisted by other persons if that assistance is necessary and reasonable. The rights and responsibilities of the occupier of the premises are also described.

Appointment of inspectors

9.22 The Authority may appoint a member of its staff or a member of the Australian Federal Police as an inspector for the purposes of the Act. It is envisaged that inspectors will require detailed knowledge of the Scheme and the ability to identify and interpret technical data, such as data used in the measurement of emissions at the facility or organisational level, which are used to calculate a liable entity's emissions number. The person must therefore have suitable qualifications and experience, and comply with any direction of the Authority. If such a direction is given in writing, it is not a legislative instrument ***[Part 19, Division 2, clause 306].*** This provision is included to assist readers, as the instrument is not a legislative

instrument within the meaning of section 5 of the *Legislative Instruments Act 2003*.

9.23 The Authority is required to issue an identity card which must be carried by the inspector. The form of the card is to be prescribed. Failure to return the card is an offence ***[Part 19, Division 2, clause 307].***

Powers of inspectors

9.24 An inspector can enter premises and exercise monitoring powers to determine whether this Act or the associated provisions have been complied with or for the purpose of substantiating information provided under the Act or associated provisions. The inspector can only enter premises with the consent of the occupier or under a monitoring warrant ***[Part 19, Division 3, clause 308].***

9.25 The monitoring powers of the inspector are specified. They include the power to search the premises and to inspect any document on the premises. An inspector may operate electronic equipment to see whether it contains relevant information. The inspector may also secure things for up to 24 hours if entry to the premises was under a monitoring warrant. This period can be extended by a magistrate ***[Part 19, Division 3, clause 309].***

9.26 Inspectors may be assisted by other persons if this is necessary and reasonable. A person assisting an inspector may enter the premises and exercise monitoring powers in relation to them but only in accordance with a direction given by the inspector. The relevant provision states that if such a direction is in writing, it is not a legislative instrument. This is to assist readers, as the instrument is not a legislative instrument within the meaning of section 5 of the *Legislative Instruments Act 2003* ***[Part 19, Division 3, clause 310]***.

9.27 Where the inspector has entered the premises with the consent of the occupier, then he or she may ask the occupier to answer relevant questions or produce relevant documents. When entry was under a monitoring warrant, the inspector may require the occupier to answer relevant questions or produce relevant documents. It is an offence not to comply with such a requirement ***[Part 19, Division 3, clause 311].***

9.28 It is not an excuse from giving an answer or producing a document in response to such a requirement that the answer or production of the document might tend to incriminate the person. However, in the case of an individual, the answer or document, the giving of the answer and producing the document, and any information, document or thing obtained as a consequence is not admissible in evidence in specified circumstances ***[Part 19, Division 3, clause 312].*** The circumstances are the

same as in the self-incrimination provision in the information gathering powers ***[Part 17, clause 300].***

9.29 Part 19 also addresses:

- Consent of the occupier, including limitations and cessation ***[Part 19, Division 4, clause 313]***
- The announcement that must be made by an inspector before entering premises under a monitoring warrant ***[Part 19, Division 4, clause 314]***
- The need to be in possession of the warrant to execute it ***[Part 19, Division 4, clause 315]***
- The requirement that the inspector provide a copy of the warrant to the occupier who is present and inform him or her of the rights and responsibilities of the occupier ***[Part 19, Division 4, clause 316]***
- Using expert assistance to operate electronic equipment ***[Part 19, Division 4, clause 317]***
- Compensation for damage to electronic equipment ***[Part 19, Division 4, clause 318].***

9.30 The occupier is entitled to observe the execution of a monitoring warrant, but not if he or she impedes the execution ***[Part 19, Division 5, clause 319].***

9.31 The occupier must provide the inspector and persons assisting the inspector with all reasonable facilities and assistance where there is a monitoring warrant applying to the premises. Failure to do so is an offence ***[Part 19, Division 5, clause 320].***

Monitoring warrants

9.32 The requirements for the issue of a monitoring warrant by a magistrate and the content of the warrant are specified ***[Part 19, Division 6, clause 321].***

9.33 The power to issue a monitoring warrant is conferred on a magistrate in his or her personal capacity. It need not be accepted but when it is exercised the magistrate has the same protection and immunity as if he or she were exercising the power as a member of the court of which the magistrate is a member ***[Part 19, Division 7, clause 322].***

Liability of executive officers of bodies corporate

9.34 Where a body corporate contravenes a civil penalty provision, and its executive officer knew that (or was reckless or negligent as to whether) the contravention would occur, the officer will be subject to a civil penalty if he or she was in a position to influence the conduct of the body corporate, in relation to the contravention, but failed to take all reasonable steps to prevent it ***[Part 20, clause 324].***

9.35 The phrase 'executive officer' is defined to mean a director, chief executive officer, chief financial officer or secretary of the body corporate ***[Part 1, clause 5, definition of 'executive officer'].***

9.36 Matters that the Court is to have regard to in determining whether an executive officer failed to take all reasonable steps include what action the person took when he or she became aware that the body corporate was contravening the civil penalty provision ***[Part 20, clause 325].***

Example 9.1

A director or chief executive officer may be aware that his or her company was failing to comply with its forest maintenance obligation and was in a position to influence this conduct, but failed to take all reasonable steps to prevent this contravention.

Example 9.2

A chief financial officer could be aware that the company was quoting a bogus OTN and receiving fuel without a carbon price, and was in a position to influence this conduct, but failed to take all reasonable steps to prevent this.

Administrative penalties and make good requirements

Unit shortfall

9.37 A liable entity may be liable because it is responsible for a facility which has more greenhouse gas emissions than the threshold amount in a particular year and for potential emissions from the fuel it supplies as an upstream fuel supplier.

9.38 Each of these will generate a provisional emissions number.

9.39 In the first year of the scheme, the sum of a liable entity's provisional emissions numbers will be the entity's emissions number.

9.40 If the liable entity does not surrender any or sufficient units by 15 December to meet its emissions number, then it will have a unit shortfall ***[Part 6, Division 3, clause 130].***

Administrative penalty and make good number – unit shortfall

9.41 An administrative penalty is imposed for a unit shortfall ***[Part 6, Division 4, clause 133].*** This is explained in more detail in Chapter 8 of this Commentary. The entity will also have a 'make good' number for the following financial year ***[Part 6, Division 4, clause 142]***. This means that it will be required to surrender additional units in relation to the following year, equivalent to the number that it failed to surrender in relation to the initial year. The aim of this mechanism is to reinforce the environmental integrity of the Scheme. Failure to surrender sufficient units in the following year will, in turn, result in a further administrative penalty and make good number.

9.42 The administrative penalty, referred to above, is calculated in accordance with the formula:

> [Number of units in the unit shortfall] x [prescribed amount for the current eligible financial year]

9.43 The amount referred to in this formula is expected to be prescribed by regulations. The maximum and default amount is 110% of the benchmark average auction price for the previous financial year ***[Part 6, Division 4, clause 133].***

9.44 The benchmark average auction price is calculated by the Authority and published on its website as soon as practicable after the end of each financial year ***[Part 6, Division 4, clause 133(3)].*** It is the higher of (a) the average auction price for units issued at all auctions in the relevant year and (b) the average auction price for units issued at the last auction in the relevant year ***[Part 6, Division 4, clause 141].***

9.45 The administrative penalty is due and payable on 31 January ***[Part 6, Division 4, clause 134]*** and from that date, a late payment penalty will start accruing ***[Part 6, Division 4, clause 135].*** The late payment penalty will be calculated on the basis of 20% per annum (or if a lower rate is prescribed, that amount) of the amount that is unpaid.

9.46 Other aspects of the surrender process are addressed in Chapter 8 of this commentary.

Administrative penalty – relinquishment

9.47 The relinquishment mechanism is also described in Chapter 8 of this Commentary.

9.48 Failure to relinquish units as required also results in an administrative penalty ***[Part 15, Division 3, clause 287].*** The administrative penalty, referred to above, is calculated in accordance with the formula:

> [Number of units required to be relinquished – number of relinquished units] x [prescribed amount for the relevant financial year]

9.49 As in the case of the administrative penalty for a unit shortfall, the penalty provisions refer to a maximum and default amount. This is 200% of the benchmark average auction price for the previous financial year ***[Part 15, Division 3, clause 287(3)]***. The reason for having a higher multiple than for a unit shortfall is that there is no make good requirement following a failure to relinquish. A make good requirement is only appropriate where there is an expectation that the entity will be a liable entity with respect to the next financial year. Relinquishment may be required in situations where no liable entity is involved, for example where a person has been issued units for the destruction of synthetic greenhouse gases on the basis of false information.

9.50 The administrative penalty is due and payable 30 days after the compliance deadline ***[Part 15, Division 3, clause 287(4)].***

9.51 From this point a late payment penalty will accrue ***[Part 15, Division 3, clause 288].***

9.52 Other aspects of the relinquishment mechanism are addressed in Chapter 8 of this Commentary.

Civil penalties

Which provisions are civil penalty provisions?

9.53 The majority of penalty provisions in the Scheme legislation are civil penalty provisions. Ancillary contraventions, such as aiding a contravention, are also civil penalty provisions.

List of civil penalty provisions

52	Mandatory quotation of OTN – large user of fossil fuels
53	Mandatory quotation of OTN – retailer of natural gas
54	Mandatory quotation of OTN – liquid petroleum gas marketer

55 Mandatory quotation of OTN – use of liquid petroleum gas as a feedstock
65 Rejection of quotation of OTN – re-supply of eligible upstream fuel
67 Misuse of OTN
68 Quotation of bogus OTN
163 Use and disclosure of information obtained from the Registry
164 Regulations about the Registry
173 Compliance with EITE reporting and record-keeping requirements
225 Reforestation reports
226 Forest maintenance obligations
235 Notification requirement – ceasing to hold carbon sequestration right
293 Notification of significant holding – controlling corporation of a group
294 Notification of significant holding – non-group entity
296 Regulator may obtain information and documents
302 Record-keeping requirements - general
303 Record-keeping requirements – quotation of OTN
304 Record-keeping requirements – rejection of quotation of OTN
324 Civil penalties for executive officers of bodies corporate

9.54 The first reason for choosing to make these civil penalty provisions is that contraventions of these provisions do not involve conduct of such serious moral culpability that criminal prosecution is warranted. Further, as most liable entities are expected to be bodies corporate, financial disincentives provided by civil penalties are likely to be most useful and effective.

Civil penalty orders – jurisdiction and amount

9.55 It is for the Federal Court to determine whether a person has contravened a civil penalty provision and to order the person to pay a penalty ***[Part 21, clause 327].***

9.56 The maximum amount of the pecuniary penalty is specified, as are the matters which the court is required to have regard to in determining the amount of the penalty ***[Part 21, clauses 327(3) and (4)].***

9.57 For the majority of civil penalty provisions, the maximum is 10,000 penalty units for a body corporate and 2,000 penalty units for other persons ***[Part 21, clause 327(4) and (6)].*** The phrase 'penalty unit' is defined by reference to section 4AA of the *Crimes Act 1914* ***[Part 1, clause 5, definition of 'penalty unit'].*** Currently, a penalty unit is $110.

9.58 Exceptions to the above maximum penalty level are:

- the penalty for quotation of a bogus OTN - the greater of

  - 10,000 penalty units for a body corporate or three times the total value of the benefits obtained from the contravention ***[Part 21, clause 327(5)]***

  - 2,000 penalty units for a person that is not a body corporate ***[Part 21, clause 327(6)]***.

- the penalty for contravening provisions relating to 'spam', based on information obtained from the Registry (clause 163)

  - 1,250 penalty units for a body corporate ***[Part 21, clause 327(4)(b)]***

  - 250 penalty units for other persons ***[Part 18, clause 327(6)(a)]***.

9.59 Penalties at the level proposed in the draft bill are needed to provide an effective disincentive against non-compliance where the financial gains from contravening obligations under the Scheme may be large. For example, the maximum penalty of 10,000 penalty units (or $1,100,000) is equivalent to 44,000 emissions units at $25 per unit, which may be a small proportion of the emissions number of many liable entities covered by the Scheme.

9.60 The possible penalty for a body corporate for quoting a bogus OTN is three times the total benefits that are reasonably attributable to the contravention ***[Part 21, clause 327(5)]***. The purpose is to ensure that the penalty directly reflects the considerable profit that could be made from quoting a bogus OTN, acquiring fuel without a carbon price and not surrendering units to the Authority as a holder of an OTN would usually be required to do.

Continuing contraventions

9.61 A person who contravenes specified civil penalty provisions which involve, for example, a requirement to do something within a particular period, commits a separate contravention on each of the days on which it fails to comply ***[Part 21, clause 338].***

Other provisions about civil penalties

9.62 While the Crown in each of its capacities will be bound by the Act, the Crown is not liable to a pecuniary penalty. This protection does not apply to authorities of the Crown or to administrative penalties or late payment penalties ***[Part 1, clause 9].***

9.63 Other aspects of the civil penalty regime are also addressed in Part 21. Of particular significance are:

- Only the Authority may apply for a civil penalty order ***[Part 21, clause 328]***

- A requirement that the rules of evidence and procedure for civil matters be applied when hearing proceedings for a civil penalty order ***[Part 21, clause 331]***

9.64 Other provisions address the grouping of proceedings ***[Part 21, clause 329]***, the 6 year time limit on initiating civil penalty proceedings ***[Part 21, clause 330]*** and the relationship between civil and criminal proceedings initiated with respect to the conduct which is substantially the same ***[Part 21, clauses 332 to 335].***

9.65 The provisions also address the situation where the person who contravenes the civil penalty provision was, for example, under the mistaken belief about facts which, if true, would mean that there would not have been a contravention of the civil penalty provision ***[Part 21, clause 336].***

9.66 Special provision is made for the state of mind of a person who does not comply with a requirement of the Authority under clause 296(4), for example, to give the Authority particular information ***[Part 21, clause 337].*** The reason for this provision is that it is reasonable to expect those subject to the provision will take steps to guard against any inadvertent contravention.

Criminal provisions

9.67 As indicated above, the provisions in the draft bill which are criminal offences are only those involving such culpability that criminal penalties are justified.

Criminal provisions

160 Making a false entry in the Registry

161 Falsified documents

307 Identity cards for inspector

311 Inspector may ask questions and seek production of documents

320 Occupier to provide inspector with facilities and assistance

340 Scheme to avoid existing liability to pay administrative penalty

341 Scheme to avoid future liability to pay administrative penalty

9.68 Entering into schemes aimed at ensuring that a body corporate or trust will, for example, be unable to pay an existing or future liability to pay an administrative penalty is a criminal offence ***[Part 22, clauses 340 and 341].*** These provisions are comparable to those which apply in relation to

various taxes. They are aimed at artificial schemes involving, for instance, 'asset-stripping'.

9.69 The maximum penalties specified in these provisions are 10,000 penalty units or 10 years' imprisonment.

9.70 Ancillary contraventions, such as aiding a contravention, are addressed by the Criminal Code.

9.71 As indicated above, the Crown in each of its capacities will be bound by the Act, but the Crown is not liable to be prosecuted for an offence. This protection does not apply to an authority of the Crown ***[Part 1, clause 9].***

9.72 In addition to the specific criminal provisions listed above, conduct in relation to the Scheme may constitute contravention of provisions of the Criminal Code. Conviction for an offence against specified provisions of the Criminal Code is one of the preconditions for a court order to relinquish units ***[Part 13, clause 280].*** The offences specified include making a statement, knowing that it is false in an application under the Carbon Pollution Reduction Scheme Act or regulations (See the consequential amendments bill, Schedule 1, Part 1, items 7-10). An example is a false statement in an application for a registry account or an obligation transfer number.

9.73 The specified provisions in the Criminal Code are also included in the list of 'associated provisions' ***[Part 1, clause 5, definition of 'associated provisions'].***

9.74 Contravention of these provisions is therefore relevant to recognition as a synthetic greenhouse gas destruction customer and an recognition as a reforestation entity. It is also relevant to the breadth of the information gathering and monitoring powers of the Authority, and to the matters which may be addressed in enforceable undertakings.

Enforceable undertakings

9.75 The Authority is empowered to accept enforceable undertakings ***[Part 23, clause 343]***. A person may, for example, undertake to take specified action directed towards ensuring that the person complies with the Act.

9.76 Such undertakings are published on the Authority's website ***[Part 23, clause 343(5)]***.

9.77 They are enforceable by the Authority in the Federal Court. The Court has a wide discretion as to the orders it can make. These include an

order directing the person to comply with the undertaking ***[Part 23, clause 344]***.

9.78 Enforceable undertakings are useful mechanisms for the Authority to help ensure compliance without necessarily taking court action.

Anti-avoidance provisions

9.79 While provisions referred to above address 'asset-stripping', other provisions address the avoidance of liability under the Scheme by artificial schemes aimed to bring facilities or activities below thresholds. A significant threshold which appears in a number of provisions in the draft bill is 25,000 tonnes of greenhouse gas emissions per facility for direct emitters.

9.80 Artificial schemes aimed at obtaining the benefit of this threshold are addressed generally ***[Part 3, Division 2, clause 23]*** and in the context of the synthetic greenhouse gas provisions ***[Part 3, Division 3, clause 30]***.

9.81 The schemes to which these provisions refer are those entered into or commenced after 15 December 2008, when the White Paper was released.

Court orders to relinquish units

9.82 Following conviction for an offence against certain specified provisions of the Criminal Code, the court may order that the offender relinquish a specified number of Australian emissions units ***[Part 13, clause 280]***. Before making such an order, the court must be satisfied that the issue of any or all of the units was attributable to the offence. The provisions in the Criminal Code which are specified include section 136.1 which relates to making false or misleading statements in an application.

9.83 A person is required to comply with such an order even if he or she is not the registered holder of any Australian emissions units ***[Part 13, clause 280(5)]***.

9.84 The procedure for relinquishment is addressed in Part 15 of the draft bill and Chapter 8 of this Commentary.

Example 9.3

SXG Ltd is a synthetic greenhouse gas destruction customer recognised under the Scheme. In November 2011, SXG applies to the

Authority for a certificate of eligible synthetic greenhouse gas destruction, and knowingly includes false information in the application, regarding the quantity of synthetic greenhouse gas destroyed. As a result, the Authority issues to SXG a certificate and 200 more emissions units than SXG is entitled to.

The fraudulent conduct is discovered and SXG is found guilty of the offence. SXG is exposed to the criminal penalty under section 136.1 (False or misleading statements in applications) of the Criminal Code. The court also orders the company to relinquish 200 emissions units. The Authority cancels the recognition of the company under clause 257(1)(a).

SXG then fails to relinquish the units by the specified time, and is further exposed to an administrative penalty of under clause 287 of the draft bill. The benchmark average auction price for 2010-11 is $26, The 'prescribed amount' for calculating the penalty is 200% of this price. The penalty is therefore $52 x 200 units = $10,400.

Chapter 10
National Registry of Emissions Units

Outline of chapter

10.1 This chapter outlines the purposes and functions of the National Registry of Emissions Units (the Registry), the rules for opening and closing accounts in the Registry, and gives an overview of the different types of Registry accounts. The chapter also outlines the circumstances in which an entry in the Registry may be corrected or 'rectified' and outlines general rules in relation to the Registry contained in Part 7 of the draft bill.

Context

10.2 The Registry serves two primary purposes:

- to track the issuance, holding, transfer, surrender, cancellation, and retirement of emissions units under the Scheme (emissions units are discussed in detail in Chapter 2 of this commentary)
- the establishment and maintenance of the registry is required to meet Australia's obligations under the Kyoto Protocol

10.3 To own and surrender units, a person must have an account in the Registry. The Australian Climate Change Regulatory Authority (the Authority) will be able to open an account for any person subject to their identity being confirmed.

10.4 Online access to the Registry will enable companies and individuals holding accounts to:

- receive units purchased at primary auctions or received via allocation
- transfer units to other account holders
- surrender units to meet Scheme obligations

- cancel units in order to help reduce emissions on a voluntary basis.

10.5 Some information held in the Registry will be published on the Authority's website and on the Liable Entities Publication Information Database. (Public information is discussed in detail in Chapter 12 of this commentary.)

10.6 Participants may trade in units for reasons other than compliance with the Scheme. They will be able to hold and transfer any type of Kyoto unit, regardless of whether it can be surrendered to meet Scheme obligations.

10.7 Companies and individuals may wish to open accounts in the Registry prior to the Scheme's commencement. The Registry will therefore be established under the executive power of the Commonwealth before the commencement of the draft bill. This will allow companies and individuals to apply to the Authority to open Registry accounts to hold Kyoto units of any type from mid-2009. Accounts to hold Australian emissions units will be available from early 2010.

10.8 Australia is required, as part of its obligations under the Kyoto Protocol and other Kyoto rules, to have a national registry to ensure accurate accounting of the issuance, holding, transfer, acquisition, cancellation, and retirement of Kyoto units. The continued existence of the Registry in the context of the commencement of the draft bill is provided for in Part 7. ***[Part 7, Division 2, clause 145]*** The remainder of this chapter outlines the provisions in Part 7 of the draft bill that will govern the Registry.

Summary

10.9 The Registry will be maintained by electronic means by the Australian Climate Change Regulatory Authority (the Authority). The Registry will have a dual function – namely, to act as a registry for Australian emission units and Australia's national registry for Kyoto units.

10.10 A person will be able to open an account in the Registry where they can hold Australian emissions units, Kyoto units and, when prescribed, non-Kyoto international emissions units.

10.11 The Commonwealth will also have a number of accounts for the purposes specified by the Kyoto rules.

10.12 A simplified outline is included in Part 7. ***[Part 7, Division 1, clause 144]***

Detailed explanation of new law

Registry

10.13 The Registry which is established under the Commonwealth's executive power before the commencement of the legislation will continue in existence after commencement of the legislation. ***[Part 7, Division 2, clause 145]***

10.14 The Registry will have a dual function – namely, to act as a registry for Australian emission units and Australia's national registry for Kyoto units. ***[Part 7, Division 1, clause 145]***

10.15 The Registry must be maintained by electronic means by the Authority. This is consistent with Kyoto rules, which requires that a Party to Kyoto's national registry be in the form of a 'standardized electronic database which contains, inter alia, common data elements relevant to the issuance, holding, transfer, acquisition, cancellation and retirement of Kyoto units.' ***[Part 7, Division 2, clause 145(2)-(3)]***

10.16 The Registry must set out the total amount of Australian emissions units in each Registry account that have the same vintage year. ***[Part 7, Division 3, clause 151]***

Registry accounts

10.17 The rules in relation to Registry accounts are contained in Division 3 of Part 7 of the draft bill. A person must have a Registry account in order to hold Australian emissions units or Kyoto units, as emissions units only exist within the electronic registry system and ownership is therefore tracked via the Registry. As the administrator of the Registry, the Authority will open registry accounts in the name of a particular person.

General rules

10.18 Each Registry account will be identified by a unique number, known as the 'account number' of the Registry account. ***[Part 7, Division 3, clause 146]***

10.19 A person may have two or more Registry accounts. ***[Part 7, Division 3, clause 146 (4)]***

10.20 A Registry account, held immediately before the commencement of the bill, will continue in existence after commencement. This ensures that a person's Registry account, and the units contained in the account, will be recognised under the bill when it

commences. (See Item 95, Part 1, Schedule 1 of the draft consequential amendments bill.)

Opening accounts - general

10.21 The Authority may, upon the request of a person, open a Registry account in the name of that person. This allows the Authority to know who the legal entity is that has opened an account and will be responsible for the units held in that account. Where a person has more than one account held in their name they may, as a non-legislative requirement, request that the Authority gives different nominated labels to each account. For example a person could register three accounts under its name, say for example Company B, and then nominate a label for each account, such as Company B – purchasing account, Company B – surrender account, Company B – voluntary surrender account. ***[Part 7, Division 3, clauses 146-147]***

10.22 The Authority may open an account in the name of a particular person where:

- the person requests the Authority to open a Registry account in the person's name in accordance with the relevant requirements contained in regulations
- the Authority has carried out the 'applicable identification procedure' in respect of the person.

[Part 7, Division 3, clause 147]

10.23 Applicable identification procedure will have the meaning as specified in the regulations. ***[Part 1, clause 5, definition of 'applicable identification procedure']*** The purpose of requiring the Authority to carry out an identification procedure is to ensure that the Authority can be satisfied of a particular person's identity before opening an account for that person.

10.24 Once a person has opened an account that person may administratively add agents to act on its behalf in relation to that account. Examples of agents that a person may wish to add include, employees of a company that have the statutory power to act on behalf of that company, brokers that have a contract with a person to act on that person's behalf and a person that has the power of attorney for the person that holds the account.

Closure of accounts – general

10.25 The Authority must close a person's Registry account if:

- there are no entries for any Australian emissions units, Kyoto units and non-Kyoto units in the account
- the person requests the Authority to close the account.

[Part 7, Division 3, clause 152]

10.26 Australian emissions units, Kyoto units and non-Kyoto international emissions units only exist electronically within the Registry system. That is, they will always be in a registry account within the (Australian) Registry or a foreign registry while they exist. Consistent with this it will not be possible to close accounts that continue to hold any units as such units cannot exist without the Registry account.

Change of a person's name

10.27 If a Registry account holder changes their name, they can apply in writing to the Authority to have their name changed in the Registry. If satisfied that the person's name has changed, the Authority must make the necessary alterations in the Registry. ***[Part 7, Division 4, clauses 153-154]***

Opening Commonwealth Registry accounts

10.28 This section outlines Australia's obligations regarding the opening of Commonwealth Registry accounts. It does not apply to companies or individuals.

10.29 The Kyoto rules stipulate that each Party's registry must contain several specific types of accounts to facilitate the tracking of units and registry transactions by the international transaction log. The mandatory account types for each national registry are:

- holding account(s). Each registry must contain at least one account for holding the Party's Kyoto Protocol units. If, like Australia has, the Party has authorised legal entities to participate in the Kyoto mechanisms, then the registry must also contain a separate holding account for each legal entity
- a retirement account into which the Party must transfer units that it intends to use to meet its Kyoto target
- cancellation accounts. Each registry must contain four distinct types of cancellation accounts:
  - a net source cancellation account that is reserved for units that the Party cancels to account for net emissions for

forestry activities under Articles 3.3 and 3.4 of the Kyoto Protocol

– a non-compliance cancellation account reserved for transfer of units when the Compliance Committee determines that the Party is in non-compliance with its Article 3.1 commitment under the Kyoto Protocol

– a voluntary cancellation account for voluntary cancellation of units not required by the Kyoto Protocol rules

– a mandatory cancellation account for cancellation of invalid units.

- Replacement accounts. Each registry must also contain at least four replacement accounts:

  – a temporary certified emission reduction replacement account to receive units used to replace expired temporary certified emission reductions

  – a long-term certified emission reduction replacement account to receive units used to replace expired long-term certified emission reductions

  – a long-term certified emission reduction replacement account to receive units to account for emissions where a long-term certified emission reduction has been subject to a reversal of storage

  – a long-term certified emission reduction replacement account to receive units used to replace long-term certified emission reductions for which a required certification report has not been submitted.

10.30 The replacement of Kyoto units is discussed in more detail in Chapter 2 of the commentary.

10.31 The draft bill provides for Commonwealth Registry accounts with designations for each of the mandatory accounts. In the event that the Kyoto rules require a further mandatory account at some point in the future it can be added to the designated Commonwealth account by regulations. ***[Part 7, Division 3, clause 148]***

10.32 New Commonwealth registry accounts can be opened at the direction of the Minister. ***[Part 7, Division 3, clause 149]***

10.33 Transitional provisions relating to Commonwealth registry accounts are included in the draft consequential amendments bill.

10.34 Kyoto units that have been transferred to a retirement account, a cancellation account, or a replacement account cannot be transferred further. For example, a Party would only transfer a Kyoto unit to the retirement account if it intended to use that unit to meet its Kyoto target. This is because it would undermine the compliance regime of the Kyoto Protocol if Kyoto units that had been retired could then be transferred for an additional use. Similarly, Kyoto units transferred to a cancellation account are for all intents and purposes cancelled, and therefore cannot be transferred to a further account. Consistent with this, the draft bill provides that Kyoto units that are in Commonwealth accounts designated as a retirement account, cancellation account, or replacement account, cannot be transferred or surrendered. ***[Part 7, Division 3, clause 150]***

Correction and rectification of Registry

Clerical errors / obvious defects

10.35 The Authority may alter an entry in the Registry for the purposes of correcting a clerical error or obvious defect. ***[Part 7, Division 5, clause 155]*** Examples of clerical errors or obvious defects include a typographical error or an entry which is clearly incorrect. The purpose of the provision is to allow the Authority to make a correction of an uncontroversial nature without having to consult the affected parties.

General power of correction

10.36 The Authority may alter the Registry in a way that the Authority considers appropriate to ensure that it accurately records the ownership of an Australian emissions unit, a Kyoto unit, or a non-Kyoto international emissions unit. ***[Part 7, Division 5, clause 156(1)]***

10.37 The Authority may exercise this power of correction where a person applies in writing to the Authority to alter an entry, or on the Authority's own initiative. ***[Part 7, Division 5, clause 156(2)]***

10.38 Before exercising this power, the Authority must advise, in writing, each person whose interests are affected by the alteration of the details of the proposed alteration(s) and give them the opportunity to make a written submission on the proposal, within a time-frame specified in the written notice. ***[Part 7, Division 5, clause 156(3)]***

10.39 If a person makes a submission within the timeframe specified in the notice, the Authority is required to take this into account in deciding whether or not to alter the Registry. ***[Part 7, Division 5, clause 156(5)]***

10.40 Where the Authority decides to alter a particular Registry entry, the Authority must publish a notice on the Authority's website setting out the details of the alteration. ***[Part 7, Division 5, clause 156(6)]***

Kyoto units and non-Kyoto international emissions units

10.41 The Authority may also make such alterations to the Registry as the Authority considers appropriate for the purposes of ensuring that the relevant provisions of the Kyoto rules or the relevant provisions of an international agreement, to the extent that the agreement relates to a non-Kyoto international emissions unit, are complied with. ***[Part 7, Division 5, clauses 157-158]***

10.42 The Authority may make the alterations as a result of a request by a person to alter the Registry, or on the Authority's own initiative. ***[Part 7, Division 5, clause 157-158(2)]***

10.43 In these circumstances, the Authority is not required to consult with persons whose interests could be affected by the alteration.

10.44 Where the Authority alters the Registry under these provisions, the Authority must publish a notice on the Authority's website setting out the details of the alteration. ***[Part 7, Division 5, clause 157-158(3)]***

Rectification of Registry

10.45 A decision of the Authority to correct an entry in the Registry is a 'reviewable decision'. This means that, if the decision is made by a delegate of the Authority, a person may apply to the Authority for review of that decision in the first instance, and may also apply to the Administrative Appeals Tribunal if the Authority affirms or varies the decision. ***[Part 24, clauses 346-348 and 350]***

10.46 A person aggrieved by one of the following matters may also make an application for rectification of the Registry to the Federal Court in respect of:

- the omission of an entry
- an entry made without sufficient cause
- an entry wrongly existing
- an error or defect in an entry
- an entry wrongly removed.

The Authority must comply with an order of the court directing rectification of the Registry. The purpose of this provision is to allow a person to apply directly to the Federal Court for an order for rectification of the Registry. This is consistent with the need for swift determination of ownership of units which the holder may wish to trade. ***[Part 7, Division 5, clause 159]***

Miscellaneous provisions

10.47 A person commits an offence if the person makes causes or concurs in the making of an entry in the Registry which the person knows is false. ***[Part 7, Division 6, clause 160]*** It is also an offence to tender in evidence a document which falsely purports to be a copy or extract from an entry in the Registry or of an instrument given to the Authority under Part 7. ***[Part 7, Division 6, clause 161]***

10.48 The purpose of these provisions is to maintain the integrity of the Registry and to ensure that it accurately reflects unit holdings and actions such as transfers.

10.49 The Authority may supply a copy of or extract from the Registry or any instrument lodged with the Authority under Part 7, certified by an official of the Authority, which will be admissible in all courts and proceedings without further proof of the original. This facilitates proceedings by avoiding the need to produce an original. ***[Part 7, Division 6, clauses 162-163]***

10.50 A person must not use or disclose information obtained from the Registry about another person to contact or send material to them, unless the information is relevant to the holding, or rights associated with the holding of, Australian emission units or Kyoto units recorded in the Registry. This is a civil penalty provision and is analogous to the limitation on the use of share registry data and is included to prevent the use of Registry data for, for example, advertising material (spam). ***[Part 7, Division 5, clause 163]***

10.51 Many actions in relation to the Registry, such as the transfer of units may be done through electronic means only. An electronic notice transmitted to the Authority is defined in the draft bill. Regulations may prescribe requirements in relation to the security and authenticity of notices transmitted to the Authority including identification checking processes and encryption of those processes. This is to give the Authority the power to determine the level of encryption and identification checking required for different actions in order to maintain the integrity of the Registry.

10.52 If an electronic notice is transmitted to the Authority it is taken to have been transmitted on the day on which the electronic communication is sent. For example an email sent at 6.45pm on Friday to Authority that waits on the server (not downloaded) until Monday morning will be taken as sent at 6.45pm on Friday. This provision is to provide certainty for the sender. ***[Part 1, clause 8]***

10.53 Regulations may make further provision in relation to the Registry. ***[Part 7, Division 6, clause 164]***

Chapter 11
Public information

Outline of chapter

11.1 This chapter relates to the various requirements in the draft bill for information to be made public.

11.2 Its focus is Part 12 of the draft bill.

Context

11.3 For units to flow to their highest value uses, their price needs to reflect all available information. This will provide a price signal that will inform business investment.

11.4 Provision of relevant market information and predictable medium-term policy will assist Scheme participants and financial market analysts to identify and understand the overall supply and demand conditions for units, allowing efficient price discovery.

11.5 Announcements by the Government and Authority about, for example, policy decisions, reported emissions and other information are of particular significance in this context. However, the decision to allow unlimited imports and surrender of certain types of international units will also be relevant to the degree of price-sensitivity of domestic announcements.

Summary

11.6 The draft bill includes provisions which will require the public disclosure of information about Scheme operations, emissions, participants and compliance.

11.7 Part 12 of the draft bill includes a simplified outline ***[Part 12, Division 1, clause 260].***

Detailed explanation of new law

11.8 Information will be made publicly available regarding liable entities, holders of Registry accounts and regarding units (Part 12).

Information about liable entities

11.9 The Authority will keep a database known as the Liable Entities Public Information Database ***[Part 12, Division 2, clause 261].***

11.10 Since liability in some situations is determined at the end of the financial year, it is not completely certain at any one point during the year which entities will be liable. For this reason, the test for inclusion on the Database is whether the Authority has reasonable grounds to believe that a person is or is likely to be a liable entity for a particular financial year. There is provision for removal of entries ***[Part 12, Division 2, clause 262(2)]*** and for correction of the Database ***[Part 12, Division 2, clause 268].***

11.11 The Database will also include the emissions number (from a report under the *National Greenhouse and Energy Reporting Act 2007* or an assessment or amended assessment of the Authority) ***[Part 12, Division 2, clause 263].***

11.12 Details of the number and types of units surrendered by each liable entity will be included on the Database ***[Part 12, Division 2, clause 266].***

11.13 Unit shortfalls will also be entered on the Database, but there is provision for annotations indicating that particular decisions are under review ***[Part 12, Division 2, clause 264].*** In addition, unpaid administrative penalties will be included ***[Part 12, Division 2, clause 265].***

11.14 The number of voluntarily cancelled Australian emissions units and Kyoto units by a person or liable entity will be entered separately on the Database ***[Part 12, Division 2, clause 267].***

11.15 The purpose of disclosing this information is to ensure that the market is fully informed about the demand for eligible emissions units.

Information about holders of Registry accounts

11.16 The Authority will publish on its website the name of each person with a Registry account and the person's address last known to the Authority ***[Part 12, Division 3, clause 269].***

11.17 The holding within an account which includes only Australian emissions units will not be published.

11.18 Further information is required by the Kyoto Rules to be published about Kyoto unit holdings. This is addressed below.

Information about units

11.19 The Authority will be required to publish information about:

- the charge per unit issued as a result of an auction and the number of units issued for that charge ***[Part 12, Division 4, clause 270]***
- the aggregate number of units issued at a fixed charge in each of the periods when this facility is available ***[Part 12, Division 4, clause 272]***
- the identity of recipients and the number of units provided free of charge under the emissions-intensive trade-exposed program, for coal-fired electricity generation, reforestation or the destruction of synthetic greenhouse gas ***[Part 12, Division 4, clause 273].***

11.20 In addition, the Authority must publish various aggregate figures:

- relating to the issue of free Australian emissions units ***[Part 12, Division 4, clause 274]***
- the surrender of borrowed and banked eligible emissions units ***[Part 12, Division 4, clause 275]***
- total emissions numbers and unit shortfalls ***[Part 12, Division 4, clause 277].***

11.21 The Authority will be required to publish the information specified in the regulations which is required to be published by the Kyoto Rules. It is also required to publish information about the total number of certified emissions reductions and emission reduction units in the Australian registry ***[Part 12, Division 4, clause 276]***.

Information about significant holdings

11.22 Where the members of a controlling corporation's group hold a total of 5% or more of the national scheme cap number for the particular vintage year, then the controlling corporation must give written notice of this to the Authority ***[Part 16, clause 293]***. In other cases, the obligation rests on the entity holding the units ***[Part 16, clause 294]***. These are civil penalty provisions which also address ancillary contraventions.

11.23 The Authority must publish the notices on its website ***[Part 16, clauses 293(6) and 294(6)].***

11.24 This provides additional information to the market which may be relevant to price.

11.25 Part 16 of the draft bill, which relates to significant holdings, includes a simplified outline ***[Part 16, clause 292].***

Other information

11.26 Other sources of information about the Scheme and its participants include:

- The Obligation Transfer Number Register ***[Part 3, Division 5, clause 49]***
- The Register of Reforestation Projects ***[Part 10, Division 13, clause 238]***
- Publication of the 'benchmark average auction price' by the Authority (which relates to setting the administrative penalty for unit shortfalls and failure to relinquish units) ***[Part 6, Division 4, clause 133(3)]***
- Publication of each certificate of eligibility for coal-fired generation assistance ***[Part 9, Division 3, clause 180(6)]***
- Publication monthly of information about the average auction price over the last 6 months (which is relevant to the adjustments to fuel taxes which will take place every 6 months) ***[Part 12, Division 6, clause 271].***

11.27 Related legislation also permits disclosure of relevant information. This includes:

- Clause 52 of the Australian Climate Change Regulatory Authority Bill, for example, will also permit the disclosure of summaries and statistics of protected information, if they are not likely to enable the identification of a person
- The *National Greenhouse and Energy Reporting Act 2007*, which is to be amended by the consequential amendments) bill.

11.28 In addition, the Authority will be required to publish a statement setting out a concise description of the characteristics of Australian emissions units and eligible international units ***[Part 12, Division 4, clause 278].***

11.29 This statement will assist in providing information to retail investors about emissions units. No product disclosure statement or prospectus would be issued by the Commonwealth under the relevant provisions of the *Corporations Act 2001* in relation to Australian emissions units.

Chapter 12
Independent reviews

Outline of chapter

12.1 Part 25 of the draft bill provides for independent reviews of the Carbon Pollution Reduction Scheme (the Scheme). A simplified outline is at ***[Part 25, Division 1, clause 352].***

Context

12.2 The Scheme is a significant, long-term reform. It is essential that regular, expert, independent and public reviews are carried out to ensure the integrity of the Scheme.

12.3 In particular, such reviews are required to provide a considered basis for periodic decisions on whether to maintain, change or extend national targets and Scheme caps.

Summary

12.4 Expert advisory committees will be constituted periodically to conduct public reviews of the Scheme. The draft bill sets out the matters such committees must address in their reviews. These include the effectiveness and efficiency of the Scheme and whether national targets relating to emissions of greenhouse gases should be changed or extended.

12.5 The first review will be completed by 30 June 2014, so that any improvements to the Scheme can be made before the start of the sixth year of the Scheme on 1 July 2015. Subsequent reviews must be carried out and completed every five years.

12.6 Expert committees must make provision for public consultation, and once a review report is complete it must be tabled in Parliament. The Commonwealth Government must also table a response to any recommendations made by the expert advisory committee. These requirements will ensure a high level of transparency and openness in the conduct of the reviews and in the Government's response to the reviews.

12.7 In addition to the periodic reviews of the Scheme, the Minister may at any time commission special reviews to investigate matters identified by the Minister.

12.8 The draft bill contains provisions directed towards ensuring that advisory committees:

- have appropriate expertise
- are independent
- are appropriately resourced.

Detailed explanation of new law

12.9 The draft bill provides for the establishment of expert advisory committees to carry out five-year, mandatory reviews of the Scheme. In addition, such committees can carry out special reviews of particular matters relating to the Scheme.

12.10 The draft bill sets out:

- timelines for periodic reviews
- the terms of reference for periodic reviews
- provision for special reviews, if required
- a requirement for public consultation
- a requirement to table review reports in Parliament
- a requirement to table responses to review report recommendations in Parliament
- provisions directed towards ensuring that review committees
  - have appropriate expertise
  - are independent
  - are appropriately resourced.

Periodic reviews

12.11 The first periodic review must be completed before the end of 30 June 2014. ***[Part 25, Division 2, clause 353(2)]***

12.12 Subsequent periodic reviews must be completed each five years, measured from the tabling of the Government's response to the previous review. ***[Part 25, Division 2, clause 353(3)]***

12.13 For the purposes of these timelines, a review is 'completed' when the report of the review is given to the Minister. ***[Part 25, Division 2, clause 353(4)]***

12.14 Periodic reviews must review certain matters set out in the draft bill ***[Part 25, Division 2, clause 353(1)]***. These matters include:

- the effectiveness and efficiency of the Scheme
- whether national targets relating to emissions of greenhouse gases should be changed or extended
- the regulations that should be made for the purposes of setting national scheme caps and gateways
- the emissions-intensive, trade-exposed assistance program
- the arrangements for the governance and implementation of the Scheme
- such other matters relating to the Scheme, if any, that the Minister specifies.

12.15 The report resulting from a review may set out recommendations to the Commonwealth Government. In formulating a recommendation for particular action, the expert advisory committee must assess the costs and benefits of the action. ***[Part 25, Division 2, clause 354(4)]***

Special reviews

12.16 In addition to the mandatory periodic reviews, the Minister may request an expert advisory committee to conduct a review of any specified matter related to the Scheme. ***[Part 25, Division 3, clause 355(1)]***

12.17 Routine reviews of administrative or operational matters may also be undertaken to ensure the effective delivery of the Scheme. No specific legislative powers are required to undertake such reviews.

Public consultation

12.18 Advisory committees must make provision for public consultation in conducting a review. ***[Part 25, Division 2, clause 353(5)] [Part 25, Division 3, clause 355(2)]***

Tabling of review reports

12.19 An expert advisory committee will provide its report to the responsible Minister. ***[Part 25, Division 2, clause 354(1)] [Part 25, Division 3, clause 356(1)]***

12.20 The Minister must, within 15 sitting days of receiving the report, cause the report to be tabled in both Houses of Parliament***. [Part 25, Division 2, clause 354(2)] [Part 25, Division 3, clause 356(2)]***

Government response to review reports

12.21 If a report makes recommendations to the Commonwealth Government, the Government must respond to those recommendations as soon as practicable. This response must be tabled in each House of Parliament within 6 months from receipt of the report***. [Part 25, Division 2, clause 354(6)-(7)] [Part 25, Division 3, clause 356(6)-(7)]***

Membership

12.22 An advisory committee must have three to five members, including the Chair. ***[Part 25, Division 4, clause 359]*** They are appointed by the Minister ***[Part 25, Division 4, clause 357]*** for the period, not exceeding five years, specified in the instrument ***[Part 25, Division 4, clause 361].***

12.23 The committee's functions are described in Part 25 ***[Part 25, Division 4, clause 358].***

12.24 The Minister can appoint acting members if there is a vacancy on the committee ***[Part 25, Division 4, clause 362(1)-(2)]***. There will be a vacancy if there are less than five members. ***[Part 1, clause 7]***

Example 12.1

Three members are appointed to an independent expert review committee. In the course of the review the Chair requests that another member with particular expertise is required. The Minister can appoint another acting member.

12.25 The Minister can also appoint an acting Chair or acting member of the committee where the Chair or member is overseas or for some other reason unable to perform their duties. ***[Part 25, Division 4, clause 362(1)-(2)]***

12.26 The Minister can grant the Chair a leave of absence, and the Chair can grant committee members a leave of absence. ***[Part 25, Division 4, clause 368]***

12.27 A member may resign his or her appointment by writing to the Minister. ***[Part 25, Division 4, clause 369]***

Expertise

12.28 The Minister may only appoint a person to an advisory committee where the Minister is satisfied that the member has substantial experience and knowledge and significant standing in at least one of these fields:

- economics
- law
- Australian industry
- climate science
- energy measurement and reporting
- greenhouse gas emissions measurement and reporting
- greenhouse gas abatement
- financial markets
- trading of environmental instruments.

[Part 25, Division 4, clause 360(1)-(2)]

Independence

12.29 Expert advisory committees are to be independent from government. To this end:

- The Chair, and a majority of members of the committee, may not be Commonwealth employees. ***[Part 25, Division 4, clause 360(3)-(4)]***

- The Minister may only terminate the appointment of a committee member on narrow grounds, including misbehaviour or physical or mental incapacity ***[Part 25, Division 4, clause 370]***

12.30 The Minister can notify expert advisory committees of relevant Commonwealth Government policies, and while the committee must have regard to those policies it is not bound by them. ***[Part 25, Division 2, clause 353(6)] [Part 25, Division 3, clause 355(3)].***

12.31 The draft bill also seeks to ensure that committee members are free from conflicts of interest. The draft bill includes:

- a general requirement that members must give written notice to the Minister of all interests, pecuniary or otherwise, that could conflict with the proper performance of the member's functions ***[Part 25, Division 4, clause 364]***

- a specific requirement that members disclose conflicts of interest to the committee, and absent themselves from any deliberation or decision with respect to that matter unless determined otherwise by the committee ***[Part 25, Division 4, clause 365]***

- a prohibition on an expert advisory committee member engaging in any paid employment that may conflict with the proper performance of his or her duties ***[Part 25, Division 4, clause 366].***

Resourcing

12.32 Advisory committee members are to be paid at a rate determined by the Remuneration Tribunal, the independent tribunal established under the *Remuneration Tribunal Act 1973* to handle the remuneration of key Commonwealth offices. Where no determination has been made by the Tribunal, committee members are paid at the rate prescribed in regulations. Members' allowances are to be prescribed ***[Part 25, Division 4, clause 367]***

12.33 Other terms and conditions (if any) are to be determined by the Minister ***[Part 25, Division 4, clause 371].***

12.34 The Authority, Department of Climate Change and other Commonwealth Departments, agencies, and authorities are given authority to assist an advisory committee. This can include the provision of information, advice, resources and facilities. ***[Part 25, Division 4, clause 372]***

12.35 In addition, the Chair of an advisory committee can directly engage consultants on terms and conditions determined in writing by the Chair. ***[Part 25, Division 4, clause 373]***

Procedures

12.36 Regulations may set out the procedures to be followed at or in relation to meetings of expert advisory committees***. [Part 25, Division 4, clause 363(1)]***

12.37 The draft bill provides the flexibility for expert advisory committees to pass resolutions without meeting, where all members are informed of the resolution or reasonable efforts are taken to inform all members of the proposed resolution. ***[Part 25, Division 4, clause 363(2)]***

Chapter 13
Review of decisions and miscellaneous provisions

Outline of chapter

13.1 This chapter addresses those provisions which provide for merits review by the Administrative Appeals Tribunal, and the miscellaneous provisions (other than transitional provisions) which are not addressed in other chapters.

13.2 It focuses on Parts 24 and 26 of the draft bill.

Context

13.3 The Government has committed to sound appeals processes for decisions under the Carbon Pollution Reduction Scheme, including judicial review pursuant to the *Administrative Decisions (Judicial Review) Act 1977* and merits review by the Administrative Appeals Tribunal.

13.4 The context of the various other provisions addressed in this chapter is included in the detailed explanation below.

Summary

13.5 The draft bill includes provision for merits review of the discretionary decisions of the Authority. It does not exclude judicial review.

13.6 The miscellaneous provisions which this chapter also addresses include further functions of the Authority, concurrent operation of State and Territory law, delegation by the Minister, alternative constitutional bases for the Scheme and commencement.

13.7 A simplified outline of Part 24, which relates to merits review, is included in the bill ***[Part 24, clause 345].***

Detailed explanation of new law

Merits review

Decisions which are subject to merits review

13.8 There is an extensive list of decisions by the Authority which are subject to merits review ***[Part 24, clause 346].*** The objective of this approach is to ensure fair treatment of all persons affected by a decision, and to encourage high quality, consistency, openness and accountability in decisions made by the Authority.

13.9 The list will not include those decisions where the Authority has no discretion.

13.10 Additional decisions will be prescribed in the regulations to be made in connection with the emissions-intensive trade-exposed assistance scheme ***[Part 24, clause 346, item 27].***

Internal reconsideration

13.11 A person who seeks the review of a reviewable decision will need to seek internal reconsideration if the decision was made by a delegate of the Authority ***[Part 24, clause 347].***

13.12 Such an application must be made within 28 days after being informed of the decision or within the period extended by the Authority ***[Part 24, clause 347(4)].***

13.13 The Authority must make a decision on the application within 90 days of receiving it ***[Part 24, clause 349].***

13.14 That decision may be to affirm, vary or revoke the decision and a written statement of reasons must be provided to the applicant within 28 days after making the reconsidered decision ***[Part 24, clause 348].***

Applications to the Administrative Appeals Tribunal

13.15 Applications may be made to the Administrative Appeals Tribunal if the Authority has affirmed or varied the decision. Where the original decision was not made by a delegate, then an application may be made to the Tribunal without the need to go through internal reconsideration ***[Part 24, clause 350].***

Stay of proceedings

13.16 The court is empowered to stay proceedings for recovery of an administrative penalty or late payment penalty while an assessment is being reconsidered by the Authority or when a decision relating to an assessment is subject to an application for review by the Administrative Appeals Tribunal ***[Part 24, clause 351].***

Miscellaneous functions of the Authority

13.17 As well as the specific functions of the Authority provided through the draft bill, the Authority will monitor and promote compliance, conduct and co-ordinate education programs and advise and assist persons (and their representatives) in relation to their obligations ***[Part 26, clauses 374(a), (b), (c), (e) and (f)]***. This is expected to be a significant part of the Authority's work in the period leading to the commencement of the Scheme and the initial years of the Scheme's operation.

13.18 The Authority will also be empowered to collect, analyse, interpret and disseminate statistical information relating to the operation of the Scheme ***[Part 26, clause 374(h)].***

13.19 This is expected to add to the body of information available to participants in the carbon market and other people who are interested in how the Scheme is operating. Other sources of information are the public information released under Part 12 and the Authority's annual report.

13.20 The Authority will also liaise with regulatory and other relevant bodies about co-operative arrangements for matters relating to the Scheme or emissions trading schemes more generally ***[Part 26, clause 374(g)].*** This liaison may be with domestic or overseas bodies, and will be important in handling the international transfers of units and will enable the Authority to learn from experience with other trading schemes.

13.21 The Authority will also advise the Minister on matters relating to the Scheme and other emissions trading schemes ***[Part 26, clause 374(d)].***

States and Territories

Concurrent operation of State and Territory law

13.22 The draft bill is not intended to exclude or limit the operation of a law of a State or Territory that is capable of operating concurrently with it ***[Part 26, clause 376].***

Arrangements with the States and Territories

13.23 The Minister is empowered to make arrangements with a Minister of a State, the ACT, Northern Territory or Norfolk Island with respect to the administration of the draft bill, including arrangements for the performance of the functions by magistrates. A copy of each instrument by which such an arrangement is made is to be published in the Commonwealth Gazette, but it is not a legislative instrument ***[Part 26, clause 378].***

13.24 Arrangements may be made with States or Territories for persons to assist the Authority (see clause 37 of the draft Australian Climate Change Regulatory Authority Bill 2009) or for magistrates to exercise power in relation to the granting of monitoring warrants ***[Part 19, Division 6, clause 321-322].***

Commonwealth

Delegation by the Minister

13.25 The Minister will be able to delegate any or all of his or her functions or power under the Act or regulations to the Secretary or a senior executive service (SES), or acting SES, employee of the Department. This power does not extend to making, varying or revoking legislative instruments. The delegate must comply with any direction of the Minister ***[Part 26, clause 375].***

13.26 The Minister has various powers under the draft bill. They include the power to direct the Authority to issue to the Commonwealth, in accordance with the Kyoto rules, a specified number of assigned amount units for a specified commitment period ***[Part 4, Division 3, clause 105].***

Executive power

13.27 The Act does not, by implication, limit the executive power of the Commonwealth ***[Part 26, clause 380].***

13.28 This is to make it clear that the bill does not, for example, limit the Commonwealth's executive power to take various actions to meet Australia's obligations under the Kyoto Protocol.

Notional payments by the Commonwealth

13.29 The Crown, in each of its capacities, will be bound by the draft bill. While the draft bill does not make the Crown liable to a pecuniary penalty or to be prosecuted for an offence, this protection does not apply to

an administrative penalty or late payment penalty under the Act ***[Part 1, clause 9].***

13.30 To accommodate this, by ensuring such amounts are notionally payable by the Commonwealth, provision is made for the Minister administering the *Financial Management and Accountability Act 1997* to give written directions relating to, among other things, transfers of amounts within or between accounts operated by the Commonwealth ***[Part 26, clause 381].***

Alternative constitutional bases

13.31 Clause 382 of the draft bill provides for the operation of the bill and the associated provisions on several alternative constitutional bases. It does this by providing for the operation of the provisions (or some of the provisions) as if they were expressly limited in certain ways - for example, as if each reference to a liable entity were expressly confined to a constitutional corporation, in reliance on the corporations power (section 51(xx) of the Constitution) ***[Part 26, clause 382]***.

Compensation for acquisition of property

13.32 If the operation of the Act or regulations would result in an acquisition of property from a person other than on just terms, the Commonwealth will be liable to pay a reasonable amount of compensation to the person. Provision is included for the institution of proceedings to recover such compensation if agreement has not been reached. The terms 'acquisition of property' and 'just terms' have the same meaning as in section 51(xxxi) of the Constitution ***[Part 26, clause 383]***.

Regulations

13.33 The draft bill includes a general regulation-making power ***[Part 26, clause 387]***.

13.34 The regulations may apply, adopt, or incorporate with or without modification, a matter contained in another instrument as it exists from time to time, despite subsection 14(2) of the *Legislative Instruments Act 2003*. The instrument referred to must be published on the Authority's website unless this would infringe copyright ***[Part 26, clause 384]***.

13.35 An example would be adoption of a matter contained in a standard published by International Organization for Standardisation, as in force from time to time.

13.36 In addition, the regulations may confer a power to make a decision of an administrative character on the Authority ***[Part 26, clause 385]***.

13.37 This provision is expected to be used in connection with the emissions-intensive trade-exposed assistance program, which will be implemented through regulations. In particular, the Authority will need to make administrative decisions about a person's eligibility for, and quantum of, assistance in accordance with the requirements in the regulations. It may also need to make administrative decisions to require the relinquishment of Australian emission units, such as on the closure of a facility ***[Part 8, Division 2, clause 168]***.

Liability for damages

13.38 Certain specified persons are not liable to an action for damages in relation to acts done in good faith (or omissions) in the performance of their functions or powers under the Act or the associated provisions. (The provision includes where such acts or omissions are done in the *purported* performance of functions or powers.) The persons include the Minister, the Authority and members of the expert advisory committee ***[Part 26, clause 379]***.

Legal professional privilege

13.39 The doctrine of legal professional privilege has been described by the High Court in *Daniels Corporation International Pty Ltd v Australian Competition and Consumer Commission* (2002) 213 CLR 543 as follows:

> "It is now settled that legal professional privilege is a rule of substantive law which may be availed of by a person to resist the giving of information or the production of documents which would reveal communications between a client and his or her lawyer made for the dominant purpose of giving or obtaining legal advice or the provision of legal services, including representation in legal proceedings."

13.40 The Act will not affect the law relating to legal professional privilege ***[Part 26, clause 377]***.

Transitional – definition

13.41 Transitional provision is made for definitions that pick up the meaning of an expression from the *National Greenhouse and Energy Reporting Act 2007*, which is being amended by the consequential amendments bill ***[Part 26, clause 386}.***

Computerised decision-making

13.42 The Authority will have the capacity to make use of a computer program for the purposes of decision making in relation to Part 10 ***[Part 26, clause 374A]***. These decisions will include calculation of the unit limit and unit entitlement in relation to reforestation. It is expected that the computer program for this purpose will incorporate an updated version of the National Carbon Accounting Toolbox. This is discussed further in Chapter 6 of this Commentary.

Simplified outlines

13.43 To assist readers, the draft bill includes a simplified outline of the Scheme ***[Part 1, clause 4].***

13.44 Each Part also contains a simplified outline of that Part's contents.

Commencement

13.45 While substantive provisions of the proposed Act will commence 28 days after Royal Assent ***[Part 1, clause 2],*** the first year in relation to which entities will be liable under the Scheme will commence on 1 July 2010. This is achieved by use of the phrase 'eligible financial year' which is defined to mean the financial year beginning on 1 July 2010 or a later financial year.

13.46 Early commencement of the proposed Act will allow liable entities and the Authority to prepare for the Scheme and for the Authority to operate the National Registry in relation to Kyoto units. Preparation will include:

- Education and assistance for entities which are likely to be liable and their representatives
- Receipt and assessment of applications for, for example, certificates of eligibility for coal-fired generation assistance, registry accounts, obligation transfer numbers, emissions-intensive trade-exposed assistance and in relation to reforestation
- The holding of at least one auction.

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Clause 331	9.63
Clause 332	9.64
Clause 333	9.64
Clause 334	9.64
Clause 335	9.64

Clause 336	9.65
Clause 337	9.66
Clause 338	9.61

Part 22: Offences relating to administrative penalties

Bill reference	***Paragraph number***
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Clause 340	9.67-9.68
Clause 341	9.67-9.68

Part 23: Enforceable undertakings

Bill reference	***Paragraph number***
Clause 342	9.5
Clause 343	9.75-9.76
Clause 344	9.77

Part 24: Review of decisions

Bill reference	***Paragraph number***
Clause 345	13.7
Clause 346	13.8, 13.10
Clause 347	13.11-13.12, 13.14
Clause 348	13.14
Clause 349	13.13
Clause 350	13.15
Clause 351	13.16

Part 25: Independent reviews

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Division 1, clause 352	12.1
Division 2, clause 353	12.11-12.14, 12.18, 12.30
Division 2, clause 354	12.15, 12.19-12.20
Division 3, clause 355	12.16, 12.18, 12.30
Division 3, clause 356	12.19-12.21
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Division 4, clause 358	12.23
Division 4, clause 359	12.22
Division 4, clause 360	12.28-12.29
Division 4, clause 361	12.22
Division 4, clause 362	12.24-12.25
Division 4, clause 363	12.36-12.37
Division 4, clause 364	12.31
Division 4, clause 365	12.31
Division 4, clause 366	12.31
Division 4, clause 367	12.32
Division 4, clause 368	12.26
Division 4, clause 369	12.27
Division 4, clause 370	12.29
Division 4, clause 371	12.33
Division 4, clause 372	12.34
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Part 26: Miscellaneous

Bill reference	***Paragraph number***
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Clause 375	13.25
Clause 376	13.22
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Clause 378	13.23
Clause 379	13.38
Clause 380	13.27-13.28
Clause 381	13.30
Clause 382	13.31
Clause 383	13.32
Clause 384	13.34
Clause 385	13.36
Clause 386	13.41
Clause 387	13.33