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Submission: Climate Change Authority Review of Emissions Reduction Fund

The ERF includes the 'safeguard mechanism' which is failing by allowing emissions to rise, undoing the modest abatement purchased under the ERF and abatement achieved in the electricity sector.

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The Australia Institute would like the following submission to the Climate Change Authority (CCA) review of the Emissions Reduction Fund (ERF).

The Australia Institute thanks the CCA for the generous extension for this submission.

The ERF is a public funded reverse auction scheme that contracts for greenhouse gas abatement. Rather than requiring emitters to pay if they emit, through the ERF the Commonwealth offers to pay emitters to emit less. The volume of Australian Carbon Credit Units (ACCUs) contracted through the scheme is relatively small and focused in the land sector. The total delivered to date is 42 Mt CO2e over five years. This is around 2% of total Australian emissions over this period.[1]

This submission focuses on the 'safeguard mechanism' (SM). The SM has long been described by government as part of the ERF. Unfortunately the SM has provided a complex means to allow emissions in most sectors to continue to rise. We urge the CCA to ensure its review of the ERF includes a thorough critique of the SM.

[1] Clean Energy Regulator (2020) *Carbon abatement contract register*, http://www.cleanenergyregulator.gov.au/ERF/project-and-contracts-registers/carbon-abatement-contract-register

The need is heightened by the recent 'King Review'[2] which proposed a number of significant changes to the SM, which the government has accepted in principle. The government has not given any credible explanation for why the King Review was needed outside of the present CCA review. Any process for developing or adopting policies proposed in the King Review should be postponed until and then informed by from the CCA's expert independent advice through this review.

More broadly, much can be said about the value and problems with the offset accreditation mechanisms, the auctioning system and source of funding, in particular its small scale, use of public funds, focus on the land sector and concerns about additionality. Some ERF proponents have even stated publicly they would proceed with projects without ERF support.[3] Nonetheless, even these problems pale in comparison with the problems with the SM.

SAFEGUARD IS PART OF ERF

The SM is an emissions trading scheme. For each facility emitting more than 100,000 t CO2e a year the SM sets an annual 'baseline', more accurately described as an emissions limit. If a facility breaches its baseline it may be liable for the excess emissions, which it can acquit using ACCUs. Facilities can also use 'flexibility' mechanisms to comply, such multi-year baselines.

When introduced the SM was explicitly intended to stop emissions from rising to undo the abatement purchased by the ERF. The Clean Energy Regulator (CER) administers the SM and describes it as an integral part of the ERF:

> To ensure these emissions reductions are not displaced significantly by a rise in emissions elsewhere in the economy, the Emissions Reduction Fund also includes a safeguard mechanism, which encourages large businesses to keep their emissions within historical levels.[4]

This page is dated June 2016. Since then the mechanism has been changed many times by changing methods for setting 'baselines'. Initial baselines were set according to metrics based on historical emissions. Updated methods set baselines according to

[2] King et al (May 2020) *Expert panel examining additional sources of low cost abatement (the King Review)* https://www.industry.gov.au/news-media/expert-panel-identifies-opportunities-to-reduce-emissions

[3] Four Corners (2019) *Climate of Change*, https://www.abc.net.au/4corners/climate-of-change/10959830

[4] Clean Energy Regulator (2016) *About the Emissions Reduction Fund*, http://www.cleanenergyregulator.gov.au/ERF/About-the-Emissions-Reduction-Fund

emissions intensity based on production (e.g. emissions per tonne of coal produced) such that baselines increase or fall in proportion to (expected) production.

The 2019 CER webpage for the SM states

> The safeguard mechanism was established as part of the Emissions Reduction Fund. … [It] complements the emissions reduction elements of the Emissions Reduction Fund by sending a signal to businesses to avoid increases in emissions beyond business-as-usual levels.[5]

Even with the shift from "historical" to "business-as-usual" baselines, the CER still directly links the ERF to the SM.

SAFEGUARD IS LETTING EMISSIONS RISE

Since the SM was introduced, total emissions covered by the mechanism have increased, as has total emissions in the sectors primarily covered by the SM.

The SM covers 'facilities' in all sectors. In practice, covered facilities are within the following sectors of the National Emissions Accounts:

- Stationary energy excl. electricity
- Transport (some rail, aviation etc)
- Fugitive Emissions
- Industrial Processes and Product Use
- Agriculture
- Waste

'Facilities' include national or state-wide operations of some companies, especially in transport.

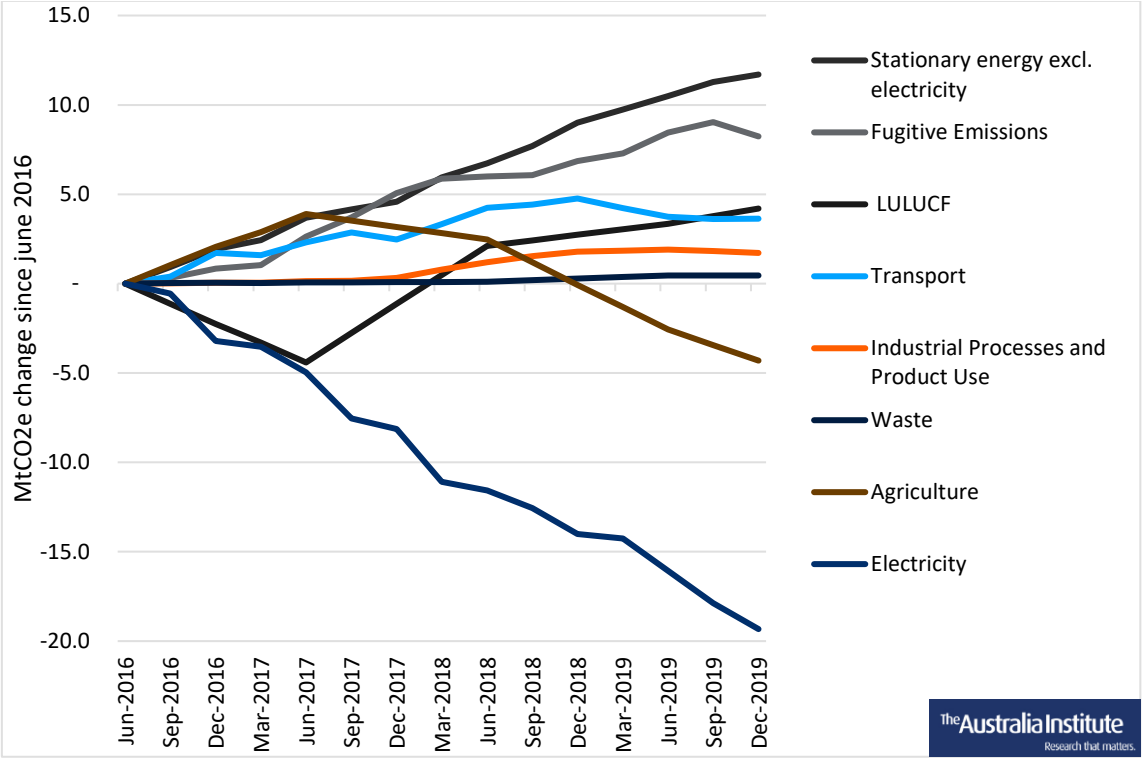
These are here described as 'SM covered sectors'.

Note that grid-connected electricity is covered by a 'sectoral baseline' which triggers compliance obligations only when the whole sector breaches the limit. Since this baseline is from 2016 and electricity emissions have maintained a clear downward trend, due to state and federal renewable energy targets and falling renewable energy costs, it has yet to be triggered.

[5] Clean Energy Regulator (2019) *The safeguard mechanism*, http://www.cleanenergyregulator.gov.au/ERF/About-the-Emissions-Reduction-Fund/the-safeguard-mechanism

In the SM sectors, since mid-2016, emissions have continued to climb (see Figure 1).

Figure 1: Absolute changes in emissions from June 2016 for each sector, year on year



Source: Analysis of Department of Industry (2020) *National Greenhouse Gas Inventory: December 2019*, https://www.industry.gov.au/data-and-publications/national-greenhouse-gas-inventory-december-2019

Here we see since the SM was introduced emissions have risen in most sectors. Other than electricity, the only other reduction has been in agriculture, ironically this is due largely to the recent severe drought. Rising emissions are making such impacts worse.

SAFEGUARD FAILURE IS CANCELLING ERF AUCTIONS

The SM covered sectors, listed above, can be combined to compare with electricity. Table 1 also compares emissions from facilities covered by SM, emissions from SM sectors and other key data from the ERF,[6] SM[7] and National Emissions Accounts.[8]

Table 1: Safeguard mechanism and ERF, key data (Mt CO2e)

	FY2017	FY2018	FY2019
Facilities covered by SM	203	211	210
Total SM reported emissions	131.3	138.4	144.0
Increase since FY2017		7.1	12.7
ACCUs from ERF	13.3	10.9	10.2
ACCUs surrendered under SM	0.4	0.3	0.2
Emissions in SM sectors	290	299	306
% of which SM covered facilities	45%	46%	47%
Total Aus emissions	529	537	536
% of which SM covered facilities	25%	26%	27%

Source: CER (2018, 2019, 2020) *Safeguard mechanism reported emissions*; DISER (2020) *National Greenhouse Gas Inventory: December 2019*; DISER (2020) *Quarterly Update of Australia's National Greenhouse Gas Inventory: December 2019*, CER Clean Energy Regulator (2020) *Carbon abatement contract register*,

[6] Clean Energy Regulator (2020) *Carbon abatement contract register*

[7] Clean Energy Regulator (2018) *Safeguard facility reported emissions 2016–17*, http://www.cleanenergyregulator.gov.au/NGER/National%20greenhouse%20and%20energy%20reporting%20data/safeguard-facility-reported-emissions/safeguard-facility-emissions-2016-17; (2019) *Safeguard facility reported emissions 2017–18*, http://www.cleanenergyregulator.gov.au/NGER/National%20greenhouse%20and%20energy%20reporting%20data/safeguard-facility-reported-emissions/safeguard-facility-emissions-2017-18; (2020) *Safeguard facility reported emissions 2018-19*, http://www.cleanenergyregulator.gov.au/NGER/National%20greenhouse%20and%20energy%20reporting%20data/safeguard-facility-reported-emissions/safeguard-facility-emissions-2018-19

[8] Department of Industry, Science, Energy and Resources (2020) *Quarterly Update of Australia's National Greenhouse Gas Inventory: December 2019*, https://www.industry.gov.au/sites/default/files/2020-05/nggi-quarterly-update-dec-2019.pdf

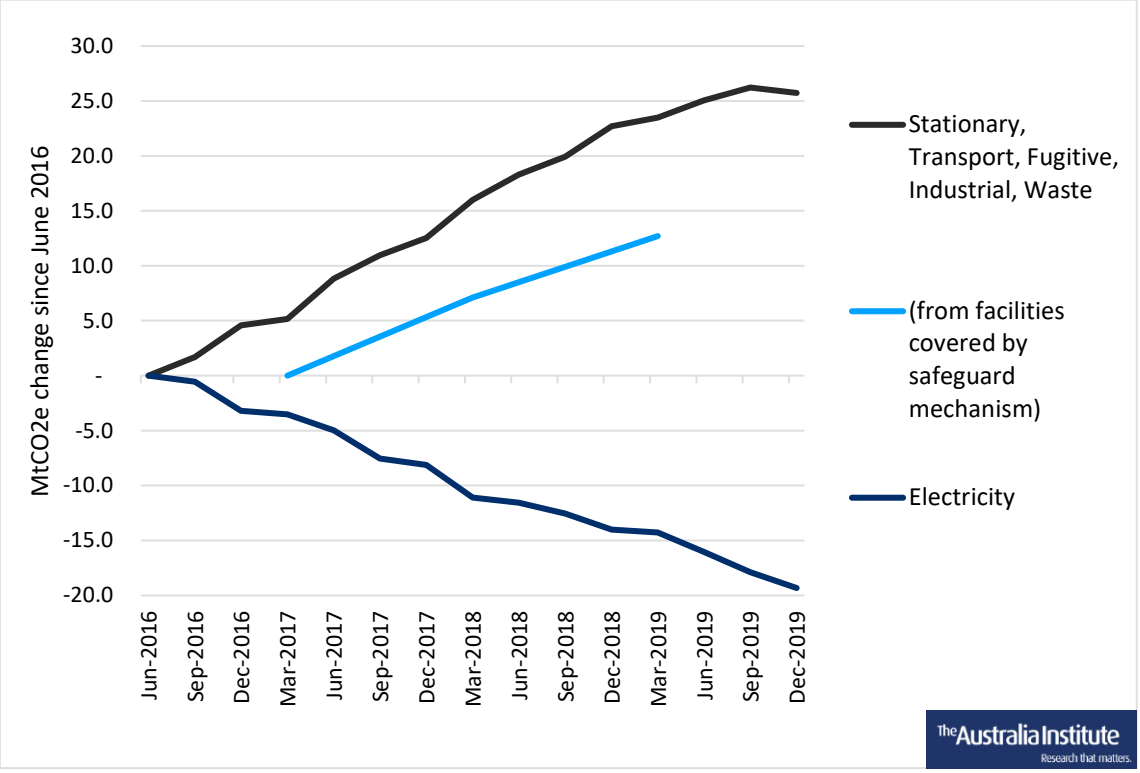
The total number of covered facilities has only slightly increased from FY17 to FY18 and actually went down in FY19, but the emissions overall have increased significantly. SM covered facilities have seen emission grow as a share of total emissions and as a share of the relevant sectors.

The emissions increase from covered facilities is now bigger than the annual ACCUs delivered under ERF. Only a tiny volume of ACCUs have been surrendered under SM.

SAFEGUARD FAILURE IS LARGER THAN ELECTRICITY ABATEMENT

The graph below shows the reductions in electricity emissions have been more than undone by the increases in emissions in SM covered sectors.

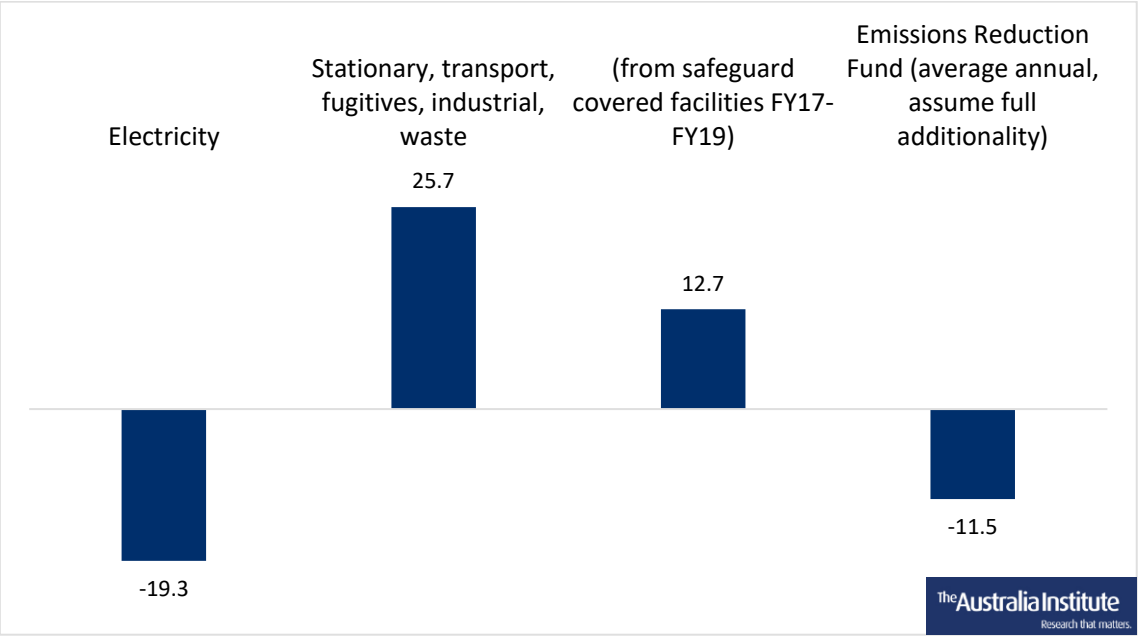
Figure 2: Safeguard allowing emissions to increase, undoing savings in electricity



Source: CER (2018, 2019, 2020) *Safeguard mechanism reported emissions,* Department of Industry, Science, Energy and Resources (2020) *Quarterly Update of Australia's National Greenhouse Gas Inventory: December 2019*

Further summary data is shown below.

Figure 3: Changes in annual emissions changes from June 2016 to Dec 2019



Source: CER (2018, 2019, 2020) *Safeguard mechanism reported emissions,* Department of Industry, Science, Energy and Resources (2020) *Quarterly Update of Australia's National Greenhouse Gas Inventory: December 2019*

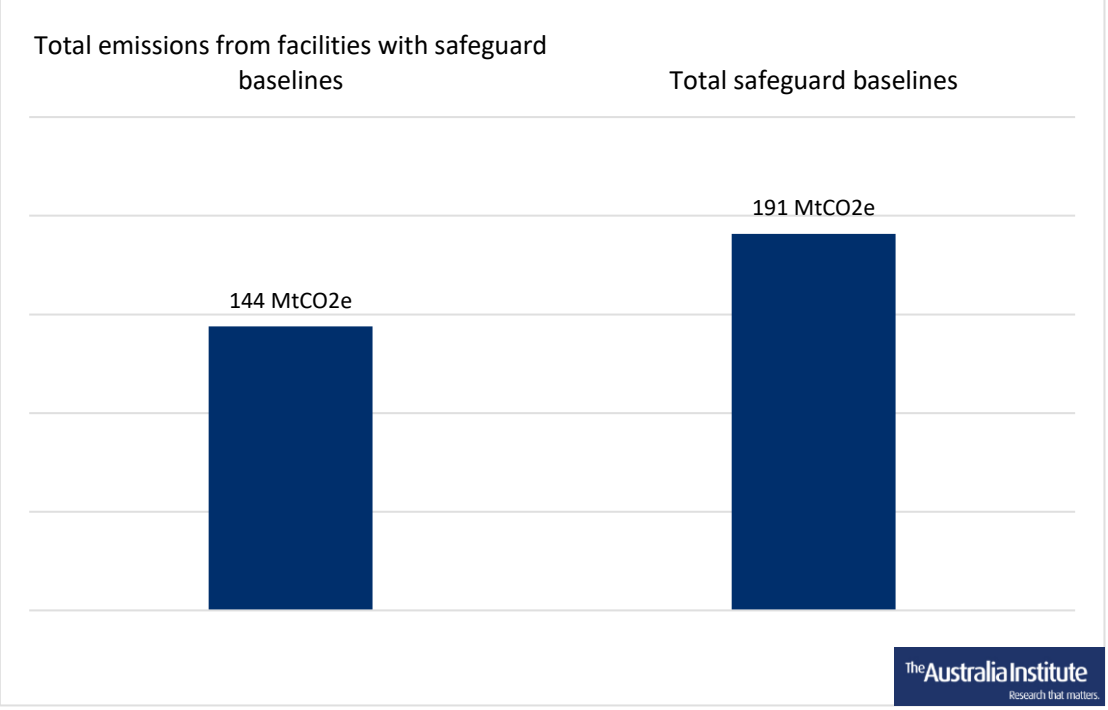
SAFEGUARD ALLOWS EMISSIONS TO CLIMB FURTHER STILL

Finally we can compare SM reported emissions with the total emission baselines.[9]

The comparison shows aggregate 'headroom' which is how much emissions at covered facilities could increase without penalty.

[9] Clean Energy Regulator (2020) *Safeguard baselines table*, http://www.cleanenergyregulator.gov.au/NGER/National%20greenhouse%20and%20energy%20reporting%20data/Safeguard-baselines-table#Safeguard-baselines-table

Figure 4: Actual emissions vs total allowed emissions from SM covered facilities



Source: Clean Energy Regulator (2020) *Safeguard facility reported emissions 2018-19*, Clean Energy Regulator (2020) *Safeguard baselines table*,

Total baselines are set at 191 Mt per year. This excludes facilities where the baseline is withheld from publication.

The emissions headroom is 32% higher than total reported emissions from facilities under the safeguard mechanism.

This is without considering future increases to baselines allowed under production-based emissions intensity baselines.

The idea that the baselines are preventing emissions from increasing even relative to 'business as usual' is simply not credible.

Moreover, Australia's emissions reduction targets are not set in intensity terms.

Finally we point to particularly conspicuous example of the problems with lax baselines: the Gorgon LNG project.

While the project was approved on condition it sequester at least 80% of reservoir CO2, the Carbon Capture and Storage (CCS) at this plant did not operate for more than three years against the Western Australian development approval conditions. Yet Chevron faced absolutely no penalty for this under the safeguard mechanism.

If the now operational CCS does continue to operate, Chevron will have in excess up to 4 million tonnes per year of additional headroom, despite not complying with its original obligations. [10]

In conclusion, the CCA review of the ERF should look closely at the SM.

It should look at ways to ensure it provides a real constraint on emissions in covered sectors to stop large emitters from continuing to push Australia's emissions up, undoing the progress in electricity.

This should be a central feature of your assessment and the Australia Institute would be happy to provide further views.

[10] Swann (2018) *Gorgon-tuan Problem*, https://www.tai.org.au/content/gorgon-tuan-problem