Trade with no cap

Submission to draft legislation for Safeguard Mechanism Credits

Expected emissions from new gas and coal projects could overwhelm any abatement from the Safeguard Mechanism.

The proposed Safeguard Mechanism legislation fails to clarify how new entrants will be managed and does not address integrity and additionality concerns around offsetting units.

The proposed legislation should not be introduced or further developed until the independent review into the integrity of carbon credits is finalised and previous consultation on the Safeguard Mechanism has been responded to.

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Summary

The proposed legislation to establish Safeguard Mechanism Credits (SMCs) should not be further developed until:

- The Government has responded to concerns raised in the initial consultation on the Safeguards Mechanism.
- The Chubb Review into the integrity problems of the existing carbon credit system has been finalised and recommendations acted upon.

These processes still need to address key concerns such as:

- How to deal with new entrants –Currently there is no limit to new high-polluting facilities entering the Safeguard Mechanism. The introduction of SMCs turns the Mechanism into effectively a cap-and-trade scheme with no cap. This is concerning given there are 69 new coal projects and 45 new oil and gas projects listed on the Office of Chief Economist Major Projects list. Just two gas projects and the 22 coal projects currently seeking EPBC approval intend to emit almost 120 million tonnes of carbon pollution to 2030, compared to the estimated abatement of the Safeguard Mechanism of 170 million tonnes.
- The integrity problems that necessitated the Chubb Review.
- The additionality of SMCs - 74% of covered facilities are already committed to reaching net zero. An additional incentive (like SMCs) will not be additional if these facilities are already on a genuine pathway to decarbonise.

Australia’s climate policy needs to move away from debate about carbon credits and offsets and towards actions that will actually decarbonise the economy. There are abundant opportunities to do this at little cost or even with economic benefit. A moratorium on new coal and gas projects, electrifying publicly-owned bus fleets and incentivising energy efficiency in commercial buildings to name just a few.

Such initiatives could be funded by an alternative fixed-price payment for above-baseline emissions. Rather than purchasing low-integrity ACCUs or SMCs an alternative voluntary ‘fixed price’ penalty payment could be established. Such a fixed price payment, set at $25 a tonne - below the current ACCU spot price - would provide certainty for major emitters, a significant source of revenue to the Commonwealth, and reduce pressure on the Clean Energy Regulator to approve low integrity ACCUs to meet rapidly growing demand.

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Introduction

The Australia Institute welcomes the opportunity to comment on the *Safeguard Mechanism Reforms (Crediting) Amendment Bill 2022* (the Bill). The Bill would allow for a new type of emissions credit, a Safeguard Mechanism Credit (SMC) which polluters covered by the Safeguard Mechanism could generate for emissions reductions. These credits could be banked to facilitate pollution in the future or traded to facilitate pollution by other facilities.

In our view the Bill should not be introduced or developed further. This consultation is not being conducted in good faith. The draft legislation to establish Safeguard Mechanism Credits (SMCs), the subject of this consultation, has been released before the outcomes of the Department's consultation on the *Safeguard Mechanism Reforms: consultation paper*.

The Consultation Paper outlined a broad range of policy options for the future Safeguard Mechanism and the use of SMCs, but did not say how either would actually operate after the reforms, nor how new fossil fuel projects were compatible with reducing Safeguard facilities' emissions. The architecture for SMCs also details possibilities for how they will be used, but without detail. These issues render this consultation illegitimate, as SMCs cannot be adequately evaluated for their merit, or otherwise, without knowing how the Safeguard Mechanism will eventually operate. For example, SMCs may lack integrity and be subject to exploitation by facilities if baselines are not determined in a way that removes all 'headroom'.

In relation to this Bill, the problems raised in our earlier submission to the *Safeguard Mechanism Reforms Consultation Paper*[1] remain:

- Australia's existing carbon credit system is deeply flawed and riddled with integrity problems. Due to the low integrity of the existing system, it is currently under review by a panel lead by former Chief Scientist Ian Chubb. No steps should be made towards creating new kinds of credits until this review is completed and its recommendations have been implemented.
- The creation of SMCs builds an opportunity and incentive for high-polluting facilities covered under the Safeguard Mechanism to exploit their baselines. It is not clear from the Bill how it will address the perverse incentives for facilities considering closure and for potential new entrants in establishing high-emitting projects.
- It remains unclear how new entrants to the Safeguard Mechanism will be treated and accommodated. Without specifying how new entrants will be limited or how the 1,227 million tonnes (Mt) carbon dioxide equivalent (CO_2e) carbon budget for the

[1] Armistead et all (2022) *Safeguarding fossil fuels: Submission to the Safeguard Mechanism Reforms Consultation paper,* https://australiainstitute.org.au/report/safeguarding-fossil-fuels/

Safeguard Mechanism to 2030 will be re-distributed when they enter, the advent of SMCs effectively creates a cap-and-trade scheme with no cap.

This is demonstrated through the estimated emissions from just two new gas projects and the new coal proposals currently seeking approval under the Environmental Protection and Biodiversity Conservation (EPBC) Act, which would produce almost 120 Mt of domestic emissions from their anticipated start date to 2030.[2] By comparison, the Department anticipates only 170 Mt CO_2e of abatement from existing Safeguard facilities to 2030 – more than two-thirds of this could be negated by fossil fuel developments.

[2] Predominantly Scope 1 emissions, with a small percentage of Scope 2 emissions included in this definition.

New Safeguard facilities

Currently there is no limit to new high-polluting facilities entering the Safeguard Mechanism. The introduction of SMCs turns the Mechanism into effectively a cap-and-trade scheme with no cap. This is concerning given there are 69 new coal projects and 45 new oil and gas projects listed on the Office of Chief Economist Major Projects list.[3]

The domestic emissions from just a handful of these projects are almost enough to overwhelm the proposed abatement from the Safeguard Mechanism, as shown in Table 1 below:

Table 1: Domestic emissions from new fossil fuel projects

	Domestic emissions - tonnes CO_2e from operation to 2030
North West Shelf Extension	53,515,000
Scarborough-Pluto	18,900,000
22 new coal proposals in EPBC process (see appendix)	44,147,124
TOTAL	116,562,124
Safeguard Mechanism proposed abatement	**-170,000,000**

Sources: WA EPA, Whitehaven Coal, Climate Analytics.[4] See Appendix

Table 1 shows that just two of the major oil and gas proposals, North West Shelf Extension and Scarborough-Pluto, could emit over 70 Mt CO_2e Scope 1 from production start to 2030. There are 43 other oil and gas projects in the major projects list. If all 22 coal mines listed in the Appendix were to proceed according to their submitted documentation, they would produce around 18.4 Mt CO_2e of Scope 1 and 2 emissions annually and a total of 613 Mt CO_2e over their project lives.

The Safeguard Mechanism has a proposed carbon budget to 2030 of 1,227 Mt CO_2e and a mandate for existing facilities to reduce emissions under the forthcoming reforms. Given

[3] Department of Industry, Science, Energy and Resources (2021) *Resource and energy major projects list*, https://www.industry.gov.au/publications/resources-and-energy-major-projects-2021

[4] Western Australian EPA (2022) *North West Shelf Extension Project* https://www.epa.wa.gov.au/sites/default/files/EPA_Report/EPA%20Report%201727%20-%20North%20West%20Shelf%20Extension%20Project%20-%20assessment%20report.pdf
Climate Analytics (2021) *Warming Western Australia* https://climateanalytics.org/media/climateanalytics_scarboroughpluto_dec2021.pdf

the total proposed abatement from the Safeguard Mechanism to 2030 is 170 Mt CO_2e, emissions from a few projects could negate a large share of the Safeguard's total abatement.

Carbon market integrity

The Bill will create the high-level architecture for a new class of carbon credits – the Safeguard Mechanism Credit (SMC). This comes at a time when the only other financial product in the carbon market, the Australian Carbon Credit Unit (ACCU), is currently being investigated due to integrity concerns.

The Government's *Independent Review of ACCUs*, led by former Chief Scientist Professor Ian Chubb (the Chubb Review), will look at integrity issues with the most popular methods used for ACCU creation, as well as how they are regulated. Importantly, it will also examine the governance arrangements which centre on the role of the Clean Energy Regulator (CER), which will also play a role in managing SMCs.

The Chubb Review will provide its report and recommendations to the government by the end of December 2022. This timeline does not allow for the outcomes of the Chubb Review to be seriously considered and addressed before this Bill is introduced.

The rushed development of SMCs risks creating another low integrity credit like ACCUs. To date, the Department has not indicated how it intends SMCs to be used by facilities and how integrity will be assured. No further work should go into the Bill until this process to assure ACCU integrity is finalised.

The Australia Institute recommends holding off on the development of SMCs, including consideration of this Bill, until all recommendations of the Chubb Review are addressed, and integrity is instilled in Australia's existing carbon market.

Abatement additionality risks

The use of SMCs also raises questions of additionality both in the context of existing facilities and new entrants.

According to Reputex, 74% of covered facilities are already committed to reaching net zero.[5] An additional incentive (like SMCs) should not be required to encourage greater abatement if the facilities are owned or managed by companies that are already on a decarbonisation pathway.

The Bill also raises the possibility for facilities that exit the Safeguard Mechanism by reducing emissions below the 100,000 CO_2e threshold to continue generating SMCs. This could incentivise facilities that would otherwise close to continue to operate to generate SMCs.

For new entrants to the Safeguard Mechanism, there is a potentially perverse incentive. Prospective new facilities with high levels of potential carbon pollution (like high-CO_2 content gas fields) could be rewarded by generating SMCs if they receive a baseline that can be easily met with the latest technology and best practice.

This raises the outstanding and largest issue with the Safeguard Mechanism – the unlimited entry for new high-polluting facilities.

[5] RepuTex Energy (2022) Potential Futures for Australia's Safeguard Mechanism, https://www.reputex.com/research-insights/report-modelling-potential-futures-for-australias-safeguardmechanism/ p. 44

Conclusion: The need for an alternative to carbon credits

Australia's climate policy needs to move away from debate about carbon credits and offsets and towards actions that will actually decarbonise the economy. There are abundant opportunities to do this at little cost or even with economic benefit. A moratorium on new coal and gas projects, electrifying publicly-owned bus fleets and incentivising energy efficiency in commercial buildings to name just a few.

For the current discussion of facilities covered by the Safeguard Mechanism, The Australia Institute's submission to the earlier consultation paper details an alternative fixed-price payment for above-baseline emissions.

Currently, Safeguard facilities purchase ACCUs to offset above-baseline emissions without restriction, with the expectation that this will be extended to SMCs. Given the extensive integrity concerns with ACCUs and the expected increase in ACCU price if integrity is restored following the Chubb Review, in addition to potentially reduced ACCU supply, an alternative voluntary 'fixed price' penalty payment could be established.

Such a fixed price payment, set at $25 a tonne - below the current ACCU spot price - would provide certainty for major emitters, a significant source of revenue to the Commonwealth, and reduce pressure on the Clean Energy Regulator to approve low integrity ACCU methodologies to meet rapidly growing demand.

This funding could be spent on decarbonisation projects elsewhere in the economy, ranging from supporting the manufacture and rollout of electric busses, batteries and renewable energy, to helping firms of all size improve their energy mix. This proposal could operate until such time as the Chubb Review concludes and integrity is restored in the carbon market.

Appendix: emissions from new coal proposals

There are at least 22 coal projects currently seeking approval under the Environmental Protection and Biodiversity Conservation (EPBC) Act that would be covered by the Safeguard Mechanism. This is not a complete list of proposed coal projects in Australia – there are likely to be others that have either not commenced the EPBC process or are expansions of existing mines that will seek modification of an existing EPBC approval.

Table 2: Coal projects seeking new EPBC approval likely covered by Safeguard Mechanism

Project Name	State	Annual product coal (mt)	Average Annual Scope 1 & 2 Emissions (t CO2-e)	Life of mine Scope 1 & 2 Emissions (t CO2-e)	Start date	Emissions to 2030
Moolarben OC3 Extension Project	NSW	8.2	549,000	5,490,000	2026	2,196,000
Glendell Continued Operations Project	NSW	4.5	433,000	6,502,698	2024	2,598,000
Mount Pleasant Optimisation Project	NSW	12.4	530,000	14,170,000	2022	4,240,000
Narrabri Underground Stage 3 Extension	NSW	11	1,480,000	33,980,000	2031	0
Ravensworth UG Mod 10 - Ashton Integration	NSW	5.6	427,000	3,416,000	2024	2,562,000
Boggabri Mod 8 - Increase in depth of mining	NSW	8.2	690,000	14,320,000	2033	0
HVO North Open Cut Coal Continuation	NSW	17.6	1,342,000	33,550,000	2025	6,710,000
HVO South Open Cut Coal Continuation Project	NSW	14.4	1,098,000	16,470,000	2030	0
Peak Downs Continuation Project	QLD	9	513,581	47,763,033	2023	3,595,067

Lake Vermont Meadowbrook Project	QLD	7	393,671	8,857,597	2023	2,755,697
Caval Ridge Mine Horse Pit Extension	QLD	6.1	371,200	11,136,003	2025	1,856,000
Ensham Life of Mine Extension Project	QLD	4.5	508,184	8,639,130	2028	1,016,368
Middlemount Coal Mine - Southern Open Cut Extension Project, QLD	QLD	4	255,612	5,879,076	2022	2,044,896
Valeria Coal Project	QLD	15	460,000	17,020,000	2024	2,760,000
Baralaba South Project	QLD	3.5	138,000	2,760,000	2023	966,000
Winchester South	QLD	11	556,000	15,600,000	2022	4,448,000
Saraji East Mining Lease Project	QLD	7	813,516	16,270,325	2024	4,881,096
Meandu Mine King 2 East	QLD	8.8	253,000	2,783,000	2024	1,518,000
China Stone	QLD	38	4,707,000	235,350,000	NA	0
Alpha North (Galilee Coal Project)	QLD	40	2,304,495	84,512,423	2030	0
The Range Project	QLD	5	301,137	7,829,562	NA	0
Blackwater Mine South Coking Coal Project	QLD	8	230,000	20,700,000	2031	0
Totals		**250**	**18,354,396**	**612,998,847**		**44,147,124**

Sources: Project documents submitted to state and Federal assessment processes and existing Safeguard Mechanism reporting

The estimates in Table 2 are based on a rapid assessment of project documents submitted to state and federal agencies. They represent a best guess at the emissions of these projects should they proceed. Many have stalled for several years and may never be developed. Where a project has stalled beyond its latest proposed start date, no start date has been estimated and no emissions to 2030 calculated. Projects may proceed at a different production rate than listed in the documents consulted depending on final approval conditions, geology and mine economics. The Australia Institute would welcome feedback from companies and assessment agencies to help refine these estimates.

Note that some of these estimates include both Scope 1 and 2 emissions. Acknowledging that the Safeguard Mechanism applies only to Scope 1 emissions, Scope 2 emissions are a limited portion of these calculation.