



3 June 2020

Climate Change Authority
GPO Box 2013
CANBERRA ACT 2601

Email: submission@climatechangeauthority.gov.au

Re: MCA submission to the Climate Change Authority (CCA) on the 2020 Review of the Emissions Reduction Fund

The Minerals Council of Australia (MCA) representing Australia's minerals exploration, mining and processing industry, supports decarbonisation of the minerals sector consistent with the climate and development goals of the Paris Agreement and based on a nationally coordinated approach to climate and energy policy.

The MCA supports the Australian Government's Emissions Reduction Fund (ERF) and safeguard mechanism as the centrepieces of Australia's climate response. The ERF has been integral in facilitating additional investments in offsetting activities while in parallel the safeguard mechanism ensures a compliance-based approach to managing Australia's emissions.

The Australian minerals sector has a longstanding relationship with Australia's offset industry as both a private sector funder of projects as well as for compliance purposes under the safeguard mechanism. The success of the ERF to deliver low-cost and reliable offsetting options relies on a stable and predictable implementation framework that supports investment certainty.

Encouraging non-land based offsets

Almost all offsets generated under the ERF and their associated Australian Carbon Credits Units (ACCUs) issued are from vegetation, waste and savanna fire management projects. While encouraging to see an increasing number of energy efficiency and industrial fugitive projects (there are about 10 waste coal mine gas power projects registered) these represent only a fraction of the offsetting outcomes (about 2.6 per cent and 1.3 per cent respectively) and ACCUs issued (about 1 per cent each).

A key challenge for the ERF is to diversify and expand the sources of offset projects to other sectors of the economy including industrial and resource sector energy efficiency, blue carbon and fugitive emissions in the minerals sector. To do so will encourage additional investments in other important offsetting activities and in turn help minimise the cost of compliance for safeguard mechanism facilities and for the economy in meeting Australia's Paris Agreement pledges.

The *Carbon Credits (Carbon Farming Initiative) Act 2011* includes emissions avoidance in its definition of offset projects. This means that a high potential offsetting option such as carbon capture and storage (CCS), which isolates emissions from the atmosphere over the long-term by capturing them from power or industrial processes and geologically storing them deep underground, should qualify as an eligible activity with an approved methodology.

The MCA notes that many experts consider CCS to be essential to meet Paris targets¹. CCS has for a decade now been recognised as an internationally accepted project-level offsetting activity under the Kyoto Protocol's Clean Development Mechanism (CDM); and its abatement can be credited through the institutional arrangements already in place under the CDM. Much practical work on CCS continues nationally by the private sector including Glencore's [CTSCo](#) (Surat), BHP, as well as organisations such as COAL21, CO2CRC and Global CCS Institute in addition to state governments. CCS is further discussed in response to the CCA's questions below.

The recent King Report recommends establishing a new process to provide third parties with opportunities to propose and prepare ERF methods. The MCA welcomes the Government's response in support of an initial scoping of a CCS/CCUS method.

Future value of Australian Carbon Credit Units (ACCUs)

ACCUs are currently trading at a spot price of around A\$16. This value is arguably insufficient to overcome the investment requirements of many non-land based offset projects.

The current demand for offsets and their ACCUs in Australia is constrained by the Australian Government's contracting of project level emissions outcomes to meet its international commitments, and private facility compliance under the safeguard mechanism to make good on capped emissions baselines.

The demand for ACCUs under the safeguard mechanism represents a fraction of the overall volume issued to date; with 77.6 million ACCUs issued since 31 December 2012 and about 535,000 surrendered under the safeguard mechanism (with about 110,000 deemed ACCUs). Without strengthening the market demand for ACCUs, their value will continue to rely on the willingness of suppliers to engage at government contracted prices; this is illustrated by the fact there are only about 4 million ACCUs registered in the Australian National Registry of Emissions Units (ANREU).

In its 2017 review of its climate change policies the Australian Government stated it will give guidance on when and how international units can be used within a context of its long-term climate strategy in 2020.

The global demand for carbon offsets could reasonably be expected to increase substantially going forward given over 95 countries have so far indicated in their Nationally Determined Contributions (NDCs) that they intend using markets to achieve their Paris Agreement pledges.

Kyoto Australian carbon credits (e.g. ACCUs) would likely be fungible within global carbon markets designed to facilitate international emissions compliance with the Kyoto Protocol and Paris Agreement (Article 6). Demand for these units could strengthen and their price attract a premium as a consequence of foreign entities looking to mitigate sovereign risk by sourcing high quality UNFCCC compliant offsets (especially as the Kyoto Protocol transitions to the Paris Agreement) and who face higher-costing abatement options.

The Carbon Credits Act states that an eligible carbon credit unit includes either a Kyoto Australian carbon credit unit or a prescribed eligible carbon unit. A prescribed unit represents abatement that Australia can potentially use to help meet its emissions reduction targets under either the Kyoto Protocol and/or its successor (the Paris Agreement) immaterial of whether it was issued in or outside Australia.

The Clean Energy Regulator (CER) is currently prohibited under the Carbon Credits Act to enter into contracts on behalf of the Commonwealth for the purchase of a prescribed eligible carbon unit. By

¹ <https://www.afr.com/companies/energy/carbon-capture-and-storage-is-essential-to-meet-paris-target-20191007-p52yak>

allowing the domestic offsets market access to international markets, Australia's ACCUs (and/or any future abatement units) might attract higher prices.

The MCA supports the Government's commitment to avoiding policies that could expose Australian export and import competing industries to carbon-related costs not faced by their overseas competitors; but it also supports Australian businesses having the choice to access credible international offsets.

The Government's principle of only allowing the use of units consistent with the implementing rules of the Paris Agreement and where they are of an equivalent standard to ACCUs (as stated in its 2017 climate policy review) may need to be revisited within the context of the Paris Agreement. The MCA observes that it remains unclear how or even if the Kyoto Protocol offsetting arrangements will transfer to the Paris Agreement's Article 6 after the Kyoto Protocol's second commitment period ends this year. This issue may be further exacerbated by recent indications within the Paris Agreement negotiations on Article 6.2 and Article 6.4 that some NDC abatement units may be subject to bilateral governance arrangements independent of the UNFCCC's rules and procedures.

Responses to questions by the Authority

The following responses broadly relate to questions in the discussion paper.

1. Views on provisions of the ERF?

It is important that a project's crediting period appropriately reflects the risks associated with maintaining the credited carbon store; and administrative crediting arrangements do not undermine the maximum incentive possible to encourage investment in the first place.

Offsets generated from CCS projects for example are unlikely to stop after 25 years and will be ongoing for a very long time; the associated abatement is internationally considered to be permanent (many thousands of years) and certainly well beyond the adopted land-based permanence of a 100 years.

The risk of emissions leaking or seeping to the atmosphere from a CCS project is scientifically considered to be low and engineering-wise technically manageable. The ERF's current imposition of a 'permanence period discount' of 20 per cent, along with a potential reversal buffer of 5 per cent for projects allocated 25 year crediting periods could prove prohibitively costly for a CCS project to proceed, as proponents do not receive the full value of their abatement.

The MCA understands that discounting was originally introduced to mitigate the potential cost to the Government of having to maintain a credited carbon store for 100 years for projects credited over 25 and subsequently discontinued; while the reversal buffer acts as a kind of insurance premium against lost carbon stores due to natural events.

Such arrangements however can (i) disadvantage abatement projects going forward relative to future program arrangements that might otherwise recognise the discounted abatement, (ii) reduce the full financial incentive through fewer issuable ACCUs, while noting (iii) these kinds of risks (including maintaining carbon stores) may lend themselves to more efficient market management options such as legally obligating proponents to make good for all emissions shortfalls through insurance products, covenants, and/or access to the international offsets market.

2. Are governance structures fit for purpose and how can abatement risk be better managed?

The MCA considers that offset schemes are highly complementary to and legitimately co-exist in conjunction with other government policies and programs that help reduce emissions as cheaply as possible. In this regard, the MCA acknowledges the CER's current [consultation process](#) on regulatory

additionality; this provision prevents offsets being credited by projects that are either required and/or being supported by existing government programs.

The MCA considers reasonable the CER's proposed approach to granting regulatory additionality to existing projects for the portion of abatement deemed additional (i.e. not otherwise likely to occur) to prevailing regulatory requirements.

In addition to what has been the ERF's exclusive reliance on reverse auctions to date, the Carbon Credits Act also provides for the CER to purchase abatement (carbon credit units) through tender and other purchasing processes; perhaps more innovative and supportive contracting approaches could be explored by the Department of Industry, Science, Energy and Resources (DISER) especially in regard to supporting non-land based offsets.

This might also include consideration of upfront crediting or deeming of ACCU's to provide a larger and more timely incentive for projects rather than retrospectively issuing ACCU's over the life of a project. The MCA also welcomes the CER's piloting at its recent 10th ERF auction of flexible 'options' contracts which provided proponents with enhanced price certainty and abatement contract flexibility.

To better support non-land based projects, including in the minerals sector, DISER could reach out and engage more closely with industry in the development of new and on-going maintenance of methods. The MCA considers for example a CCS methodology could be developed relatively quickly for consideration by the Emissions Reduction Assurance Committee given the existing and long-lived international institutionalisation of CCS under the Kyoto Protocol.

3. Opportunities for enhancing outcomes

The ERF offers businesses an opportunity to minimise their compliance costs of exceeding baselines under the safeguard mechanism through the acquittal of both deemed and/or over the counter (OTC) purchases of ACCUs; while offering project proponents a valuable revenue stream through government contracting and/or the sale of ACCUs in primary and secondary markets.

It is also clear that the ERF facilitates broader environmental co-benefits such as avoiding deforestation, protecting biodiversity through savannah burning and potentially blue carbon, and enhancing ecosystem resilience. The MCA notes and supports the King Report's identification of accelerating a blue carbon method as being highly worthy of development.

The recent and devastating bushfires have prioritised within the national conversation a greater focus on enhanced adaptive capacity and resilience to climate change impacts. The ERF's contracting arrangements already include a force majeure clause; however some land-based activity contracts may need to be cancelled or renegotiated due to the fire damage.

This suggests there is inherent vulnerability built into the current ERF portfolio mix, and much benefit to be derived from diversifying projects beyond just land-based projects while still recognising the importance of them.

The enhancement of the fund's ability to provide for a broader range of projects such as non-land use activities could further bestow important cultural, regional and economic benefits. But the focus of the ERF should remain on CO₂ abatement and not on the monetising of non-CO₂ co-benefits.

Closing observations

The MCA notes that the ERF has been reviewed extensively in recent times by the Australian National Audit Office in 2016, the Climate Change Authority in 2017, the Department of the Environment and Energy in 2017, and more recently the King Report and the Clean Energy Regulator.

It remains the MCA's view that the ERF is a well-designed, well-governed domestic offset scheme that is currently performing well given its stated purposes of (i) removing and/or avoiding emissions in order to meet Australia's obligations under international agreements; (ii) creating incentives for offsetting projects; and (iii) reducing emissions while protecting the environment (among others).

There is opportunity to transition the ERF to be less risk averse without losing abatement integrity by allowing project proponents to realise the full economic benefit of their abatement outcomes and transferring abatement risk to the market rather than embedding it in the administration of the fund.

The fund should also focus on incentivising non-land based offsetting activities where appropriate, especially CCS, energy efficiency, blue carbon and fugitive emissions in the minerals sector. This is strongly consistent with the findings of the King Report.

Finally, accessing much larger international offsets markets could help deepen Australia's domestic offsets markets and help ensure the future sustainability of the ERF by increasing the demand for ACCUs.

Yours Sincerely

A handwritten signature in blue ink, reading "Tania Constable". The signature is fluid and cursive, with a large loop at the beginning.

**TANIA CONSTABLE PSM
CHIEF EXECUTIVE OFFICER**