

Committee Secretary
Senate Standing Committees on Environment and Communications
PO Box 6100, Parliament House
Canberra ACT 2600
By email: ec.sen@aph.gov.au

25 January 2023

Dear Committee Secretary,

RE: Senate Inquiry into the Safeguard Mechanism (Crediting) Amendment Bill 2022 – call for submissions

The National Environmental Law Association Ltd ACN 008 657 761 (NELA) welcomes the opportunity to contribute to the Senate Inquiry into the Safeguard Mechanism (Crediting) Amendment Bill 2022 (SMC Amendment Bill).

1. NELA's objects and its interest in this Senate Inquiry

NELA is a peak body for advancing Australian environmental law. It is a national, multidisciplinary, member-based association focused on environmental law and sustainability. NELA is managed by a national board that includes Directors with expertise in international and domestic legal frameworks for biodiversity conservation, climate change and natural disasters, environmental regulation and regulatory theory and natural resource management.

One of NELA's core objectives is to provide a forum for, and to otherwise assist in, the discussion, consideration and advancement of environmental law across the legal profession and the wider community. NELA is also a member of the leadership committee of the Professional Bodies Climate Action Charter Australia and New Zealand Forum, which represents professional members in Australia across a wide range of sectors from finance, insurance, science, engineering, law, health, construction and the built environment. Given the potentially significant influence that the legislated SMC Amendment Bill and the introduction of Safeguard Mechanism Credits (SMCs) more specifically may have on Australia's emissions reduction efforts, the Bill is of key concern for NELA's members. NELA is grateful for the opportunity to make a submission to this Inquiry.

2. Background to this submission

Under the Paris Agreement, Australia is required to assist in the global effort of limiting global warming to well below 2 degrees Celsius, and preferably 1.5 degrees Celsius compared to pre-industrial levels. Australia's Nationally Determined Contribution (NDC) as prescribed under the *Climate Change Act 2022* (Cth) (CC Act) commits it to achieving net zero emissions by 2050 and a target of 43 per cent below 2005 levels by 2030. To meet these legislated targets, urgent reform is necessary. NELA echoes its submission to the Department of

Industry, Science and Resources (**DISER**) made on 20 September 2022 titled ‘Safeguard Mechanism Reform: Consultation Paper’,¹ where NELA stated its support for recommendations made by the Climate Change Authority (**CCA**) that an ‘enhanced safeguard mechanism’ is a ‘pragmatic and durable way of reducing emissions across a range of industrial, manufacturing and resource sectors’.

Indeed, while highly politicised, monetising greenhouse gas pollution presents a beneficial method of managing emissions. Although NELA supports the ultimate creation of a comprehensive emissions trading scheme, the safeguard mechanism (**SM**) has the potential to make an important temporal contribution to furthering Australia’s efficient and commercially competitive transition to net zero. Particularly, the introduction of Safeguard Mechanism Credits (**SMCs**) provides a useful market-based incentive for emissions reduction by allowing the issuing of tradeable SMCs for participants operating facilities that match or surpass Australia’s climate targets. The SMC Amendment Bill creates the operational framework for SMCs by amending the *National Greenhouse and Energy Reporting Act 2007* (Cth) (**NGER Act**) and the *Australian National Registry of Emissions Units Act 2011* (Cth) (**ANREU Act**). The bill outlines how SMCs are to be issued, purchased, and included in Australia’s National Registry of Emissions Units. NELA also reaffirms its support for the implementation of the broader and more ambitious Roadmap for Climate Reform.²

NELA recognises that introducing the SMC Amendment Bill’s proposed amendments into parliament is a government priority necessary to ensure the viability of their passage into law prior to the scheduled commencement date of the SM. However, we note that many key design elements of the SM are not included in the SMC Amendment Bill and will instead be a topic of government consultation on the National Greenhouse and Energy Reporting (Safeguard Rule) 2015 (**Safeguard Rules**). Provided this, NELA’s comments on the SMC Amendment Bill are subject to revision upon the commencement of the Safeguard Rules consultation.

3. Summary of comments and recommendations

- NELA supports the redrafting of the NGER Act objects to better reflect Australia’s national and international greenhouse gas emissions reduction targets prescribed by the CC Act;
- NELA submits that reform of the second object of the NGER Act should go further to prescribe a rate at which emissions should decline overall to provide more certainty and accountability. The emissions decline rate prescribed should be that required to achieve Australia’s greenhouse gas emissions reductions targets and move towards the goal of the Paris Agreement;

¹ National Environmental Law Association, ‘Safeguard Mechanism Reform: Consultation Paper’ (20 September 2022) <<https://www.nela.org.au/wp-content/uploads/Safeguard-Mechanism-Consultation-Paper-Final.pdf>>.

² Environmental Defenders Office, ‘A Roadmap for Climate Reform’ <<https://www.edo.org.au/publication/a-roadmap-for-climate-reform/>>.

- NELA supports the introduction of provisions which reasonably fetter the discretion of the Minister and Regulator to safeguard the integrity of SMCs. NELA submits that the NGER Act should prescribe the key elements of SMCs to limit the Regulator’s discretion. This would better guide the Regulator’s currently broad power to issue SMCs;
- NELA submits that the NGER Act should implement reforms which ensure that SMCs harness the highest integrity standards including legislating clear timeframes within which the scheme should be independently reviewed, and mechanisms for triggering reform if shortfalls or weaknesses in the scheme are identified. NELA also supports the imposition of a tight limit on the number of carbon credits that a facility can purchase to meet its obligations and the inclusion of a mechanism similar to the former *Energy Efficiency Opportunities 2006* (Cth) which compelled major energy users to audit their operations for opportunities to reduce demand;
- NELA supports the SMC Amendment Bill’s inclusion of a provision which bases penalty amounts on the amount of damage caused to the climate by excess emissions. Whilst NELA supports this approach, it suggests a viable alternative approach which corresponds with proposed provision 22XNI;
- NELA supports the proposal in the SMC Amendment Bill explanatory note to increase transparency surrounding ACCU and SMC holdings in Registry accounts;
- NELA submits that an option for smaller facilities falling below the designated large facility threshold to opt-in to the SM should be introduced;
- NELA supports the inclusion of more robust auditing requirements for facilities providing reports under sections 19, 22G, 22X or 22XB of the NGER Act and provisions made for the relinquishment of issued SMCs as a result of false or misleading information. NELA submits that the CCA should periodically review the integrity of SMCs and the contributions the credits are making in emissions reduction efforts;
- NELA supports the consistent legal framework proposed by the SMC Amendment Bill for the handling of ACCUs and SMCs;
- NELA supports the statement made in the SMC Amendment Bill explanatory note that a core element of the reforms to the SM will be a framework where baselines decline predictably and gradually over time in order to support strong emissions reductions being delivered by Safeguard facilities; and
- Rather than implement proposed amendments to the NGER Act that will make it possible to transfer SMCs issued into a holding account so that they can be provisioned to emissions-intensive trade-exposed (EITE) facilities, NELA supports the more tailored approach to assisting EITE facilities proposed in the Safeguard Mechanism Reforms Position Paper (**Position Paper**).

4. Comments and recommendations

NELA supports the redrafting of the NGER Act objects to better reflect Australia's national and international greenhouse gas emissions reduction targets prescribed by the CC Act. Australia's climate policy to date has been contradictory, piecemeal and generally insufficient. To ensure the efficacy of Australia's future climate policy and law, legislation must consistently reflect Australia's greenhouse gas emissions targets in its objects. The CC Act already prescribes one of its objects as being to 'set out Australia's greenhouse gas emissions targets which contribute to the goals of holding the increase in the global average temperature to well below 2 degrees Celsius above pre-industrial levels and pursuing efforts to limit the temperature increase to 1.5 degrees Celsius above pre-industrial levels'. However, this cannot be the sole avenue for expressing and making headway in achieving these ambitions. Instead, coordinated legislative reform to express and achieve these goals is necessary, particularly in the context of the Powering Australia Plan which emphasises that the SM holds key responsibility for achieving the CC objects.

Clear objects are especially necessary in the context of the SM, which is largely regulated by subordinate legislation. Legislated objects will help to ensure that Australia's new emissions reduction targets inform the interpretation and enforcement of all aspects of the revised NGERS Act, including by operators of EITE facilities, decision makers and courts. Clarification of legislated objects may also mitigate opportunity for delegated authorities to fail to execute their duties consistently with overarching objects which have had the benefit of parliamentary scrutiny.

While NELA supports the reform of the second object of the NGER Act, it also submits that the reform should go further to prescribe a rate at which emissions should decline overall to provide more certainty and accountability; to the Parliament, the Australian electorate, markets, and the global community to which Australia must report its progress under the Paris Agreement. The emissions decline rate prescribed should be that required to achieve Australia's greenhouse gas emissions reductions targets and move towards the goal of the Paris Agreement.

NELA supports the introduction of provisions which reasonably fetter the discretion of the Minister and Regulator to safeguard the integrity of SMCs. NELA supports the introduction of Item 37 which states that the Minister must not make Safeguard rules unless satisfied that those rules are consistent with the second object of the NGER Act. This inclusion places a necessary fetter on Ministerial discretion to ensure that safeguard rules are made consistently with the parliamentary intention underlying the SM. This limitation realigns ministerial discretion to accord with changes made to the objects of the NGER Act.

In saying this, NELA submits that further reform should be implemented to better guide the Regulator's currently broad power to issue SMCs. As it stands, this power to issue units to persons in relation to a facility prescribed under section 22XNA(1) is only to be limited, if at all, by the Safeguard Rules which may make provision for, or in relation to, the issuing of SMCs by the Regulator under section 22XNA(2)-(3).

To ensure that the issuing of SMCs is consistent with the broader legislative framework, NELA submits that the NGER Act should also prescribe the key elements of SMCs to limit the Regulator's discretion. Key elements should include that one SMC, equivalent to one tonne of greenhouse gas emissions, will be issued for greenhouse gas emissions which fall below a facility's baseline and that a facility's net emissions number will be reduced by one tonne of greenhouse gas when it surrenders one SMC. These key elements are consistent with the recently released Positions Paper which allows emitters under the SM to both automatically earn SMCs where emissions fall below the baseline to incentivise abatement initiatives and trade SMCs to offset emissions and reduce net emissions.³ Alternatively, and at a minimum, the Regulator's power to issue SMCs should be subject to limitations prescribed in the Safeguard Rules which correspond to and are consistent with the objects of the NGER Act.

NELA submits that the NGER Act should implement reforms which ensure that SMCs harness the highest integrity standards. Integrity should be a key concern when introducing legislative instruments to regulate SMCs, particularly given the public's concerns surrounding the management of Australian Carbon Credit Units (ACCUs). To further ensure the integrity of SMCs, NELA reiterates its submission made on 20 September 2022,⁴ emphasising the need to legislate clear timeframes within which the scheme should be independently reviewed, and mechanisms for triggering reform if shortfalls or weaknesses in the scheme are identified. To ensure high-integrity standards, NELA supports the recommendations made by the Climate Council in its Power Up report which include:

- imposing a tight limit on the number of carbon credits that a facility can purchase to meet its obligations to ensure that the scheme is oriented towards 'achieving absolute emissions reduction rather than simply facilitating large-scale carbon offsetting';
- avoiding any perverse incentives or regressive subsidies and instead encouraging 'facilities to achieve the greatest possible emissions reductions, both within the current reporting period and over the longer term'; and
- considering a mechanism similar to the former *Energy Efficiency Opportunities Act 2006* (Cth) which compelled major energy users to audit their operations for opportunities to reduce demand. This would 'deliver outsized benefits if paired with a government funded clearing house for information about emissions reduction opportunities and grant funding for facilities covered by the Safeguard Mechanism'.

³ Safeguard Mechanism Reforms, 'Position Paper' (January 2023) < https://storage.googleapis.com/files-au-climate/climate-au/p/prj23cd662ff4387d8c254ae/public_assets/Safeguard%20Mechanism%20Reforms%20Position%20Paper.pdf>.

⁴ National Environmental Law Association, 'Safeguard Mechanism Reform: Consultation Paper' (20 September 2022) <<https://www.nela.org.au/wp-content/uploads/Safeguard-Mechanism-Consultation-Paper-Final.pdf>>.

NELA supports the SMC Amendment Bill's inclusion of a provision which bases penalty amounts on the amount of damage caused to the climate by excess emissions. In the SMC Amendment Bill, this is achieved by basing penalties for excess emissions situations 'on both the size of the excess emissions situation and the number of days in which the excess emissions situation exists'.⁵ This approach received further support in the Positions Paper, which proposes to update civil penalties to reflect both the number of days of exceedance and the quantity of excess emissions.

While NELA supports this approach, it recognises the viability of an alternative approach which corresponds with proposed provision 22XNI which addresses penalties for failure to meet relinquishment requirements. If this approach was adopted, upon exceeding a baseline, an offender would be required to pay the greater of \$20 or 200% of the market value of an SMC for each tonne of emission exceeding their baseline. This approach will ensure that facilities are deterred from emitting beyond their baselines and will promote consistency and clarity surrounding the issuance of SM offence penalties. Whichever approach is adopted must be strictly enforced where a breach has occurred and the effectiveness of this change hinges on sufficient resources and powers for the relevant agency.

NELA supports the proposal in the SMC Amendment Bill explanatory note to increase transparency surrounding ACCU and SMC holdings in Registry accounts. NELA reaffirms its submission made on 20 September 2022 which states that regulated operations must be subject to continuing reporting obligations and transparent calculations of annual estimated emissions (made publicly available), so that baselines can be set in a way that is consistent with those estimates, scrutinised, and tightened over time. This transparent approach will ensure the viability of determining baselines at Safeguard facilities by using site-specific emissions intensity values based on actual production levels, to ensure baselines reflect changing productivity values as proposed in the Positions Paper.

In saying this, NELA recognises the importance of addressing stakeholder concerns regarding public reporting on the ACCU and SMC holdings of individual account holders due to, for example, the information being commercially sensitive and of a constantly changing nature. As such, NELA supports amendments made to the bill to address these concerns which provide that the legislative rules may require the Regulator to publish specified information about ACCU or SMC holdings for which there are entries in Registry accounts and the registered holders of such units on the Regulator's website. This amendment will allow further consultation to ensure an appropriate balance is reached between increasing transparency, and addressing concerns made by stakeholders.

⁵ Explanatory Memorandum, Safeguard Mechanism (Crediting) Amendment Bill 2022
<https://parlinfo.aph.gov.au/parlInfo/download/legislation/ems/r6957_ems_bef2a383-93a0-4d6b-85a0-6c2b0850008e/upload_pdf/JC008241.pdf;fileType=application%2Fpdf>.

NELA submits that an option for smaller facilities falling below the designated large facility threshold to opt-in to the SM should be introduced. This option would provide a market-incentive for smaller facilities to decrease emissions, allowing them to generate SMCs and contribute to decarbonisation efforts while increasing SMC trade opportunities for hard-to-abate facilities. The addition would also signal (and provide valuable evidence about) the potential to expand the SM in the future. The introduction of an opt-in option for smaller facilities aligns with, but moves beyond, the SMC Amendment Bill's amendment of section 15B of the NGER Act, which enables a person other than a controlling corporation or responsible emitter for a designated large facility to register to report under the NGER Act. As recognised in the explanatory note, this amendment could be used to allow facilities to continue to generate SMCs if they are no longer covered by the SM and are not covered by existing registration provisions in the NGER Act.

NELA supports the inclusion of more robust auditing requirements for facilities providing reports under sections 19, 22G, 22X or 22XB of the NGER Act and provisions made for the relinquishment of issued SMCs resulting from false or misleading information. These auditing requirements assist in ensuring that SMCs issued under the SM are of the highest integrity. NELA looks forward to reviewing the details of when audits might be required which will be provided for in the Safeguard Rules. NELA also supports the SMC Amendment Bill provisions relating to false or misleading information or reporting, which are similar to provisions for the relinquishment of ACCUs outlined in the *Carbon Credits (Carbon Farming Initiative) Act 2011 (Cth) (CFI Act)* and will also assist in ensuring integrity. Building upon the need to foster integrity, NELA submits that the CCA should periodically review the integrity of SMCs and the contributions the credits are making in emissions reduction efforts. A situation where a lack of transparency transpires partly due to requirements of non-disclosure as has been seen in the context of ACCUs and Clean Energy Regulator non-disclosure provisions in the *Clean Energy Regulator Act 2011 (Cth) (CER Act)* should be avoided.

NELA supports the consistent legal framework proposed by the SMC Amendment Bill for the handling of ACCUs and SMCs. The SMC Amendment Bill clarifies that SMCs will be subject to the same regulation as ACCUs in respect of their registration, transfer and surrender. This consistent dealing will ensure the development of an efficient decarbonisation pathway for the industrial sector and will broaden market supply.

NELA supports the statement made in the SMC Amendment Bill explanatory note that a core element of the reforms to the SM will be a framework where baselines decline predictably and gradually over time in order to support strong emissions reductions being delivered by Safeguard facilities. This proposition was most recently addressed in the Positions Paper, which encouraged the introduction of a hybrid baseline model with baselines to be reduced in the short term at an average baseline decline rate of 4.9% each year to 2030 for all safeguard facilities (excluding EITE facilities).

Rather than implement proposed amendments to the NGER Act that will make it possible to transfer SMCs issued into a holding account so that they can be provisioned to EITE facilities, NELA supports

the more tailored approach to assisting EITE facilities proposed in the Positions Paper. This approach involves providing financial assistance to trade exposed facilities which is external to the scheme and allowing trade exposed facilities to apply for a lower baseline decline rate to moderate potential scheme costs. The lower baseline decline rate will depend on how impacted a particular facility is. This approach will ensure that the integrity of the scheme is maintained and mitigate the potential lowering of credit numbers available to facilities operating under their baselines.

5. Conclusion

As a final comment, NELA emphasises the need to ensure a consistent approach to SMC implementation and regulation on a state and federal level. Consistent state and federal approaches to SMCs will ensure that facilities are not tasked with interpreting and attempting to act in accordance with complex compliance regulations prescribed at national and sub-national levels.

The SMC Amendment Bill has the potential to meaningfully contribute to urgent emissions reduction efforts recognised domestically and internationally through capitalising on market-based incentives. NELA has welcomed the opportunity to comment on the SMC Amendment Bill and looks forward to the commencement of the Safeguard Rules consultation.



Madeline Simpson

NELA Director, for the NELA Board