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**EMISSIONS REDUCTION FUND GREEN PAPER**  
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20 February 2014

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Emissions Reduction Fund Submissions  
Department of the Environment  
GPO Box 787  
CANBERRA, ACT 2601

Dear Sir

The Australian Sustainable Business Group (ASBG) welcomes the opportunity to comment on *The Emission Reduction Fund Green Paper*.

The [Australian Sustainable Business Group](http://www.asbg.net.au) (ASBG) is a leading environment and energy business representative body that specializes in providing the latest information, including changes to environmental legislation, regulations and policy that may impact industry, business and other organisations. We operate in NSW and Queensland and have over 130 members comprising of Australia's largest manufacturing companies. Members were fully involved in the development of this submission and ASBG thanks them for their contribution.

ASBG strives to assist regulatory agencies to prepare more efficient regulatory process, with the outcome of achieving practical, efficient, low cost solutions to achieve high environmental outcomes.

## Overview

ASBG agrees with the general thrust of the Government's action in the introduction of the Direct Action program, but is concerned over the increased administrative burden and the effectiveness of the scheme.

There are some good potential opportunities for the Government to design an effective scheme which can take advantage of international trade in carbon credits. Given the considerable shrinkage of manufacturing in Australia, the sale of carbon credits, due to the downturn, on international markets is an opportunity which needs exploration. ASBG acknowledges, this comes with many strings attached, but may help in reducing the financial burden of the ERF.

The Emissions Reduction Fund (ERF) is potentially prone to complex baseline and measurement metrics which can vary considerably over the industry sectors chosen. Efforts to streamline these metrics will benefit both the Government and business sectors. Hence, use of the current measurement practices such as NGER, or other current systems is encouraged.

The Government is to replace the Carbon Pricing Scheme, which is a cap and trade scheme, with the Direct Action policy, which includes the Emissions Reduction Fund (ERF). The focus of this submission is on the ERF and its basic design.

## Use of Absolute Emissions for the Baseline

Most of the issues with the ERF centre on its basic design. A baseline and credit scheme (B&CS) has a number of challenges to overcome for it to be an effective process to reduce greenhouse emissions.

One of the major issues with a B&CS is its traditional focus on energy intensity, though the Green paper discusses both emissions intensity and absolute as potential options.

ASBG supports a combination of both an absolute baseline and energy intensity baseline. An absolute baseline is where the total emissions in CO<sub>2-e</sub> in tonnes per annum are used.

ASBG considers a B&CS using two baselines would solve many issues such as, administration costs, measurement and alignment with NGERs and international carbon markets.

ASBG's model is to use two baselines:

- An **absolute baseline** in tonnes CO<sub>2-e</sub> tonnes for a base year is set
- Credits are paid on tonnes CO<sub>2-e</sub> made below this absolute baseline
- An **energy intensity baseline** is also set
- Penalties are triggered if the energy intensity falls below the intensity baseline and on emissions that exceed the absolute baseline
- Penalties can be based on a rolling average of an international carbon credit price (e.g. EU ETAs)

The advantage of this arrangement of scheme includes:

- Consistency with international carbon credit schemes based on CO<sub>2-e</sub> tonnes
- Credits are paid only on real reductions from absolute baseline, not from an intensity baseline. This removes the issue of increased emissions due to increased production, but where energy intensity is below the baseline.
- Credits are permitted to be sold on the international market
- Provides a gap where middle performance is not credited nor penalised
- Measurement of the absolute baseline to be linked to NGER amounts removing some of the administrative complexity
- Baselines to be linked to the NGER 4 methods measurement process, simplifying the improvement measurement process
- A maximum auction price can be based on international credit amounts
- Economic impacts of variations in the emission intensity baseline are less critical

Disadvantages include:

- Non-NGER participating applications will need to be consistent with the NGER approach and require additional administrative expense
- Administrative costs of calculating both the absolute and emissions intensity will remain (but the latter not as financially critical)
- Non-NGER applicants will be required to be subject to the NGER process with special determinations drafted for this purpose
- The high administrative cost for non-NGER bids will deter smaller scale projects
- Difficulties in making international arrangement for ERF credits

The following table describes the issues arising with B&CS and possible means to overcome these.

**Table 1 Emissions Reduction Fund Issues and Possible Improvements.**

Issue Name	Description	Possible Improvements
Consumers not affected	Baseline and credit schemes do not necessarily penalise emissions intensive activities and goods, thereby muting the incentive to consumers to buy less emissions intensive good or undertake less emission intensive activities	<p>This is purposefully done reflecting the Government’s policy of reducing the costs to consumers, including businesses, of a carbon reduction process. Consumers will only indirectly feel the cost of the scheme via the tax system and allocation of government spending, but this will not provide any price signals on specific products, such as electricity.</p> <p>However, the Government could introduce permit use of a trademark which identifies products which are under the scheme to identify to consumers which Australian companies are winning bidders. This is a soft marketing program and reflects the ‘green energy’ programs currently available.</p>
Increased Administrative Costs	Under a baseline and credit system, a baseline has to be set for each emitting activity, usually based on historical emission and production rates. This means that the administrator has to establish a base line for each activity at each facility (generating plant, mine and industrial plant).	<p>Use of ASBG’s model should reduce administrative costs for NGER liable organisations as the absolute baseline can be generated from NGER data.</p> <p>The emissions intensity baseline can then be estimated from production levels. As only penalties apply for not reaching both baselines, only programs that fall within an error margin of performance would need verification to see if penalties apply. Reduction in the verification process to a margin of performance will further reduce the administrative burden. Though the defining of a production unit can be challenging, but once negotiated it will be established in the contract.</p> <p>It is noted this opportunity is not available for non-NGER liable sites and organisations. For consistency reasons use of the NGER measurement methods for non-NGER proposals would be used to ensure a consistent approach.</p>
Baseline development complexities	<p>Linked to administrative costs the setting of baselines will be a complex and costly task.</p> <p>Establishing industry sector baselines will be a complex and a negotiate outcome with winners and losers.</p>	<p>ASBG’s model removes much of the complexities of being solely reliant on an intensity baseline. NGER based companies will be in a more predictable position in the setting of baselines.</p> <p>Organisations outside NGER will be a far more difficult task due to the lack of verified emission data.</p> <p>Baselines can be linked to the NGER’s 4 level measurement process. This means improvement to the accuracy to the baselines can be made subject to the choice of the participating program to change its measurement practice along NGER lines. How retrospective the credits due will need to be negotiated considered at the contractual level.</p> <p>Non-NGER programs will be more difficult to develop, but the NGER process can be used as a default for establishing the baselines.</p>

Issue Name	Description	Possible Improvements
Contractual complexities	Winning bidders will enter into contracts with the government to receive credits based on performance criteria. Contracts will also contain penalties for failing to meet performance levels. Complex verifications will be necessary.	<p>Some organisations may under bid on their credit price and cannot complete their obligations. Withdrawal from the scheme may be appropriate in such examples, with a reasonable penalty applied. External unforeseen factors may also lead to underperformance. These could include state regulation or international legal or other contractual issues.</p> <p>Where projects are subjected to unforeseen genuine issues slowing down the ability to reach the target, use of purchase of international credits could be provided in the contract.</p>
Relation of emissions intensity to total reductions	Standard B&CS assumes the use emissions intensity only, rather than total emissions. This causes complexities in the conversion of intensity credits to emission credits. This approach also makes it less certain in being able to meet international targets such as Kyoto or others which may be set in the future.	ASBG's model of the use of absolute baseline for provision of credits in CO <sub>2-e</sub> /t will generate credits consistent with international markets.
Ability to use international credits	With an indirect link between emission intensity and total emissions trade on international markets of tonnes of CO <sub>2-e</sub> could be limited.	<p>ASBG's model helps aligns with international carbon credit schemes and measurement practices.</p> <p>If credits are provided in CO<sub>2-e</sub>/t units, there is a possibility that the ERF could be made stable enough for it to be accepted for international trade.</p> <p>The Government should explore the possibility where high credit earning programs can benefit from international credit sales based on credits issued under the ERF. ASBG acknowledges that this will require careful design of the ERF credit system to satisfy the international conditions for acceptance. The potential benefit is such credits could be in part paid for by foreign interests rather than the Australian tax payer.</p>
Additionality issues	The auction process favours lowest priced emissions reductions, but this can include programs which would be implemented without ERF assistance. It also rewards laggards as sites which have already invested in energy efficient practices have higher marginal costs for the next project.	<p>Many sites liable under the NGER, the Carbon tax and EEO will have already undertaken multiple energy efficiency projects. Hence, their energy saving projects will tend to have higher marginal costs. Also the absolute baselines for NGER sites will be already known under the scheme and easier to assess for additionality and setting of baselines.</p> <p>The area of complexity and concern is for non-NGER entities and the administrative costs for assessing additionality for this sector.</p> <p>Placing Internal rate of return limits on projects will be administratively difficult and subject to rorting.</p>
Auction Prices	Many organisations may shy away from the scheme early as they wait for more certainty on the prices set at the auctions. There is a financial risk of application failure without knowing likely range of winning bids.	Publication of the winning price or the range of the top 3 bids will provide industry sectors a better idea of likely credit per tonne CO <sub>2-e</sub> to strive for. This can be published after the first rounds and be used to vary the Clean Energy Regulator's benchmark price.

Issue Name	Description	Possible Improvements
Single or low number of industry sectors dominate the auction prices	Some industry sectors or project types can have significant natural cost advantages. For example methane capture from landfills. Hence, will dominate and absorb the limited funding under the ERF.	<p>The Government has already set a precedent of selecting industry sectors for allocations of the Direct Action funds. The agricultural sector has a substantial allocation already. Hence, this implies that funding to various industry sectors will be considered. The advantage of this is it will remove the ability of one sector to dominate the funding. The disadvantage is that the lowest cost projects will not be chosen, only those within the industry sector and capped at a funding amount.</p> <p>Given that Direct Action has already limited funding according to industry sector then this should continue in a broad manner to provide ERF opportunities in various sectors.</p>

Overall the Green paper on the ERF appears to be looking for answers rather than providing a firm framework. As such, ASBG has provided its set of ideas to assist in the ERF's development.

Should you require ASBG to clarify or elaborate on the above matter please contact me.

**Yours Sincerely**

A handwritten signature in black ink, appearing to read 'Andrew Doig', written over a light grey rectangular background.

**Andrew Doig**  
**CEO**

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