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FOR CURTIN

## Safeguard Mechanism Submission

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## Introduction

My electorate is very concerned that we build a regulatory framework that will drive the decarbonisation of our economy.

The Safeguard Mechanism must play a crucial part in helping Australia meet its current emissions reduction targets of 43% by 2030 and net zero by 2050 and increase the ambition of those targets over time to ensure that Australia plays its part in a pathway to a liveable planet.

I note the Safeguard Mechanism commenced on 1 July 2016, but the current regulations have not been effective in driving substantive emissions reductions.

I commend the Government for reviewing the Safeguard Mechanism with the intention of giving it 'teeth'. It is a complex regulatory tool and ongoing analysis and adjustment will be required to ensure that it is incentivising the necessary changes and not creating unintended consequences.

A significant issue in designing the Safeguard Mechanism is the calculation of baselines. I propose a hybrid model – setting absolute baselines but using industry average emissions intensity factors for the initial baseline calculation. While this adds complexity in the short-term, it does not penalise early adopters and creates a simpler and more effective mechanism over the longer term.

I make this submission after consultation with experts within and beyond my electorate. I look forward to working constructively with the Government, industry and the community, to make our transition to a decarbonised economy effective, efficient and fair.

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## Summary of Recommendations

1. The 100,000 tonne CO<sub>2</sub>-e threshold should be decreased progressively so the Safeguard Mechanism covers a larger proportion of emissions and facilities do not become exempt through reducing their emissions.
2. Annual reductions from covered facilities collectively need to at least match their percentage of overall emissions to ensure equity.
3. Absolute baselines should be used as they are more effective, equitable, efficient and simple than emissions intensity baselines. But absolute baselines could be set using an industry-average emissions-intensity measure, so early adopters and efficient facilities are not disadvantaged.
4. Annual reviews of the Safeguard Mechanism will assess progress towards targets and allow decline rates to be adjusted, if necessary, as well as accommodating a larger national share of emissions as the threshold is lowered to cover more facilities.
5. Headroom should be removed for Phase 1 based on the most recent available data on recorded emissions.
6. Absolute baselines should be set for existing facilities using most recent production data and industry-average emissions intensity data.
7. Emissions from new entrants should be included in the overall emissions budget. New entrants should either fully offset their emissions, so the additional emissions reduction burden is not shifted to another company or sector, or the Clean Energy Regulator could create an 'emissions allowance' in its annual review by increasing reduction targets for other facilities.
8. The interaction between SMCs and ACCUs requires significant analysis to ensure the complexity does not create unintended perverse incentives and liquid markets drive efficient and effective reductions.
9. Limited banking and borrowing arrangements within a particular Phase should be implemented.
10. Deemed surrender should be removed.
11. No use of international credits should be permitted until the international market is more developed, with proven high integrity carbon credits
12. In order to incentivise the required decarbonisation of the economy, exemptions for EITE businesses should be very limited and focused on industries that will be essential in a net zero world.
13. Additional funding to EITEs should be used very sparingly.
14. The Powering the Regions Fund should be used at an industry level to support innovation and just transition.
15. EITEs should not be directly provided with SMCs.
16. EITEs should not be given differential decline rates.
17. Multi-year monitoring periods should not be used as they add unnecessary complexity.
18. The decline trajectory to 2030 requires absolute baselines, headroom to be removed and linear decline rates with regular reviews, for all covered facilities.
19. Absolute baselines remove significant complexity, including the need to calculate production variables on an ongoing basis.
20. Legacy emissions from landfills should be included at some stage (with an appropriate baseline adjustment), triggering SMC generation.
21. Options to renegotiate baselines should be removed and penalties imposed on facilities that exceed their baselines.

## Background

The Safeguard Mechanism is intended to restrict the emissions of Australia's biggest polluters. Properly implemented, it will play a crucial part in helping Australia meet its emissions reduction targets of 43% by 2030 (relative to 2005 levels) and net zero by 2050.

Industrial facilities that emit more than 100,000 t CO<sub>2</sub>-e Scope 1 (direct) emissions per year are subject to baseline limits on the amount of CO<sub>2</sub>-e they are allowed to produce. If the baseline is exceeded, the emitter can purchase or generate and surrender Australian Carbon Credit Unit (ACCU) offsets or apply to have their baseline adjusted or waived. The 100,000 tonne threshold covers about 215 individual facilities in mining, oil and gas extraction, manufacturing, transport and waste.

Since its introduction in 2016, the Safeguard Mechanism has failed to reduce industrial emissions. Instead, emissions have increased as baseline limits have been set far above actual emissions, due in part to the practice of individual facilities negotiating their baselines with the Government. Where baselines have been breached, an Australian Conservation Foundation investigation found that no facility has ever been penalised by the Clean Energy Regulator for the breach.

The Government's *Safeguard Mechanism Reforms Consultation Paper August 2022* (**Consultation Paper**) invites discussion on some key areas for strengthening the Safeguard Mechanism but does not draw attention to several weaknesses of the current scheme. This submission responds to the questions posed in the Consultation Paper.

In developing this submission, proposals have been assessed using the Consultation Paper's stated policy principles of **effective** (achieving targeted reductions), **equitable** (fairly distributing the burden), **efficient** (allowing the market to find lowest cost solutions) and **simple** (making administrative and reporting requirements as straightforward as possible).

Of primary importance is a return to fixed (absolute) baselines, rather than the current production-adjusted (intensity) baselines. Absolute baselines are most effective, equitable, efficient, and simple, as will be demonstrated below.

## Response to Consultation Paper Questions

### 1. The Safeguard Mechanism's share of the national abatement task

#### *What should the Safeguard Mechanism's share of Australia's climate targets be?*

For Australia to achieve its emissions reduction target of 43% (relative to 2005 levels) by 2030, annual emissions must reach 354 Mt CO<sub>2</sub>-e in 2030, down from 621 Mt in 2005 and 497 Mt in 2020. This figure can also be expressed as a carbon budget of 4,381 Mt CO<sub>2</sub>-e from 2021-2030. Framing the target as a budget is useful because it allows trade-offs between actions now and actions in future years to be better recognised.

The Safeguard Mechanism currently only applies to facilities that produce more than 100,000 t CO<sub>2</sub>-e per annum. If the Safeguard Mechanism can be reformed to be an effective emissions reduction tool, then increasing the emissions covered by the scheme will allow it to have greater impact. This could be done in multiple ways.

1. The 100,000 tonne CO<sub>2</sub>-e threshold should be decreased progressively so the Safeguard Mechanism covers a larger proportion of emissions and facilities do not become exempt through reducing their emissions.

The threshold for inclusion could be lowered to encompass more facilities and retain coverage over existing facilities as emissions decrease. As baselines drop and emissions decrease, existing facilities will eventually fall under the 100,000 tonne threshold. To maintain the effectiveness of the scheme, the threshold must be lowered progressively. This will also allow the inclusion of new facilities into the scheme, so that more than 28% of emissions are covered and the regulatory framework has a greater chance of driving the emissions reductions required. Lowering the threshold will require a recalculation of the Safeguard Mechanism budget based on the new percentage share of national emissions.

2. Annual reductions from covered facilities collectively should at least match their percentage of overall emissions to ensure equity.

In 2020, the Safeguard Mechanism covered 137 Mt CO<sub>2</sub>-e, or 28% of national emissions. This 28% could be used as the basis of the Safeguard Mechanism target emissions reductions, i.e. the covered facilities will bear their 'fair share' of emission reductions. As the Safeguard Mechanism is the primary enforcement mechanism to achieve reduction targets, this seems like a reasonable principle.

However, the discussion paper does not contain enough detail on how this would play out, or how a changing proportion of national emissions or increased reduction targets would be managed.

A reassessment mechanism will need to be devised that does not reward facilities covered by the Safeguard Mechanism for delaying emissions reductions, individually, at an industry level or for the covered facilities as a whole. It will need to ensure that low-emissions sectors of the economy do not bear the burden of Australia's biggest polluters.

The Government should provide modelling on emissions reduction trajectories at the national and Safeguard Mechanism level to inform this mechanism, with particular focus on effectiveness and equity.

## 2. Setting baselines to achieve an equitable distribution of costs and benefits

### 2.1 Fixed (absolute) versus production-adjusted (intensity) framework

*Should we retain, and build on, the existing production-adjusted (intensity) baseline setting framework or return to a fixed (absolute) approach?*

3. Absolute baselines should be used as they are more effective, equitable, efficient and simple than emissions intensity baselines. But absolute baselines could be set using an industry-average emissions-intensity measure, so early adopters and efficient facilities are not disadvantaged.

Arguments about productivity must not lose sight of the goal of productivity economy-wide, not just in Safeguard Mechanism facilities. A productive decarbonised economy will inherently see growth in low and zero carbon industries and contraction or phasing out of high-carbon activities.

Without absolute baselines, it is difficult to see the link between the Safeguard Mechanism and the 43% emissions reduction target. Adding new emissions-efficient facilities still adds emissions and will prevent targets from being met, unless those facilities replace emissions-inefficient facilities.

The challenge of absolute facility baselines based solely on historical emissions, is that they do not reward early adopters or more emissions-efficient facilities for improvements made during the initial 5 years of the Safeguard Mechanism's operation.

I would propose that absolute baselines be set, based on industry average emissions intensity and actual production data.

This will ensure facilities that have already reduced their emissions are not penalised, but also link baselines to the achievement of targets.

In the first year, this will require a more complex calculation to be undertaken in the setting of baselines. Rather than using default emissions intensity values (which are now up to 10 years old), current industry averages should be calculated, to avoid creating unnecessary headroom.

SMCs will initially be created for the half of facilities that are below industry average emissions intensity. It is possible that this may cause already-efficient facilities to temporarily stall further improvements but it will also require bigger reduction efforts from high-intensity emitters from the start. Given that baselines are absolute and not based on intensity going forward, and will be reducing every year, any initial SMCs are likely to be used rapidly.

This approach is likely to be popular with the more emissions-efficient facilities in each sector, as it rewards them for previous action, and less popular with the more emissions-intensive facilities.

These absolute baselines will then need to be ratcheted down over time, linked to the 43% emissions reduction target, or more ambitious targets, as agreed in line with international commitments.

4. Annual reviews of the Safeguard Mechanism will assess progress towards targets and allow decline rates to be adjusted, if necessary, as well as accommodating a larger national share of emissions as the threshold is lowered to cover more facilities.

With a default linear decline rate, I would propose an annual review, where the Clean Energy Regulator can make adjustments to the linear decline path. In doing this, the Clean Energy Regulator would assess progress towards targets over the last year, potential new entrants that are deemed essential (and for whom the rest of the covered facilities therefore need to 'make room'), and any changes to the proportion of covered emissions as a share of total national emissions.

This annual review could supplement reporting to Parliament by the Climate Change Authority on progress towards targets and would be like the Fair Work Commission setting the wage rate or the RBA setting interest rates.

**Absolute targets, calculated to favour more emissions-efficient facilities at the start and reviewed annually to track progress, would actually provide a pathway to achieving emissions reduction targets.**

The use of absolute baselines calculated with reference to industry average emissions intensity will achieve the aims of the Safeguard Mechanism in the following ways.

**Effective** - Absolute baselines reflect the total amount of emissions produced, which is the only meaningful way to assess progress towards our carbon budget and national emissions reduction goals. Production-adjusted baselines only reduce CO<sub>2</sub>-e per production unit, allowing total emissions to increase as production increases. If production-adjusted baselines are used year on year, they are unlikely to actually lead to meeting targets.

**Equitable** - Setting the absolute baseline with reference to industry average emissions intensity will ensure early adopters will not be penalised. A facility's growth is then contained within the envelope of an absolute baseline, or needs to be offset above the baseline, providing more certainty about reaching targets and ensuring that the facilities covered by the Safeguard Mechanism as a whole are reducing their fair share of emissions.



Decarbonising the economy necessarily requires shifts from some industries and producers to others. This approach creates a level playing field to ensure that economic incentives are aligned with a forward-looking economy.

**Efficient** - Absolute baselines are most efficient in supporting decarbonisation across the economy as they will level the playing field for new and existing green industries. The role of high-emitting industries will necessarily diminish in a decarbonised economy. If these facilities cannot reduce their total emissions and increase productivity at the same time, they will not be competitive over the long term.

**Simple** – The initial setting of absolute baselines by reference to industry average emissions intensity is more complicated than setting absolute baselines linked to historical emissions. But once they are set, absolute baselines are much simpler for facilities to report and monitor and simpler for a regulator to link to desired targets. The initial complexity is justified by the improved effectiveness and longer-term simplicity.

Absolute baselines also avoid creating incentives for facilities to individually negotiate, which is not equitable, efficient or simple and risks being seen as being politically motivated. Current arrangements allow facilities to individually negotiate an adjustment to their baseline after the relevant year has concluded. This should not continue.

## 2.2 Headroom and the need to remove it

*Views are sought on the proposal to reset baselines in a way that removes aggregate headroom so crediting and trading can commence when baselines start to decline.*

5. Headroom should be removed for Phase 1 based on the most recent available data on recorded emissions.

Current baselines are set far above actual emissions, so that facilities can increase emissions without consequence. Removing this headroom as soon as possible is vital to making the Safeguard Mechanism fit for purpose and most recent available data on recorded emissions is the fairest way to do this. Crediting and trading is a beneficial effect of reducing headroom (see Section 3).

Current headroom will need to be removed by recalculating average emissions-intensity factors for each industry. Some headroom for specific facilities will remain using the baseline calculation method described in 2.1 above, but if baselines are absolute and declining, this headroom should be consumed quickly.

## 2.3 Setting baselines for existing facilities

*What is the preferred approach for setting baselines for existing facilities? Approaches may include:*

- *Option 1: setting all baselines using industry-average benchmark emissions-intensity values.*
- *Option 2: setting all baselines using facility-specific emissions-intensity values.*

- *Other proposals, noting there are many possible approaches.*

6. Absolute baselines should be set for existing facilities using most recent production data and industry-average emissions intensity data.

An absolute baseline could be set based on recent production data and industry average emissions-intensity data, as follows:

Facility baseline = # units produced last year x emissions/unit (industry average)

That could then become an absolute emissions cap and future production expansion must occur within the envelope of that absolute cap, as it is adjusted in accordance with targets year by year. The decline rate for facility baselines would be linear in principle but reviewed annually to ensure that collective progress towards the Safeguard Mechanism's carbon budget is being met, with adjustments made according to the outcomes of the previous year. This annual review would also be an opportunity to factor in new facilities covered by a decline in the 100,000 t CO<sub>2</sub>-e threshold.

## 2.4 Setting baselines for new facilities

*What are the advantages of best practice, industry average benchmarks or alternative approaches for setting baselines for new entrants, noting that a final decision will be informed by baseline setting arrangements for existing facilities?*

7. Emissions from new entrants should be included in the overall emissions budget. New entrants should either fully offset their emissions, so the additional emissions reduction burden is not shifted to another company or sector, or the Clean Energy Regulator could create an 'emissions allowance' in its annual review by increasing reduction targets for other facilities.

The primary question in setting baseline arrangements for new entrants is:

**If a new high-emissions project is approved, which companies or industries will be expected to reduce their emissions more to make room in the carbon budget?**

The options are:

- a. New projects must fully offset their emissions;
- b. Other covered facilities must increase their emissions reduction targets;
- c. The additional emissions reductions must be achieved by activities not covered by the Safeguard Mechanism; or
- d. The new projects are treated as being 'outside' the 43% emissions reduction target.

I would propose that the only feasible options are (a) or (b).

In its annual review, the Clean Energy Regulator could carve out an 'emissions allowance' for new entrants, where those new entrants are seen as being an important part of a net zero economy. If this decision is made, it should be made clear what this means for the emission reduction targets for the rest of the covered facilities.

If no emissions allowance is granted by the Clean Energy Regulator, new entrants should be required to fully offset their emissions, so the additional emissions reduction burden is not implicitly shifted to another company or sector.

This will deter new entrants into high emission industries. This is what is needed to stay within the emissions budget. Extensions to existing projects should be treated the same as new entrants, and not permit the Safeguard Mechanism's total emissions cap to increase.

### 3 Crediting and trading, domestic offsets and international units

The proposed automatic allocation of SMCs to facilities emitting within their baseline is an efficient and simple way to encourage emissions reductions.

*Are there any other issues to consider with the proposal to allow the Clean Energy Regulator to automatically issue tradable credits to Safeguard facilities whose emissions are below their baseline, with crediting and trading commencing on 1 July 2023 subject to baseline setting arrangements that remove aggregate headroom?*

8. The interaction between SMCs and ACCUs requires significant analysis to ensure the complexity does not create unintended perverse incentives and liquid markets drive efficient and effective reductions.

The current Chubb review of ACCUs will not hand down its findings until December 2022. Decisions about how SMCs operate and interact with ACCUs must be informed by these findings.

The simpler the system, the more likely it is to drive efficient and effective outcomes. Care will need to be taken to ensure that ACCUs are not compromised or that SMCs are granted without being 'earned'. A review mechanism will need to be built into this trading framework as it is likely to need ongoing improvements as proponents and facilities find loopholes.

Using an intensity-linked absolute baseline mechanism (see 2 above), in the initial year, the SMCs created will not necessarily directly correlate with a carbon 'offset'. But over the medium term, as absolute baselines are ratcheted down, SMCs and ACCUs will become more inter-changeable and their price should converge.

Assuming that the Chubb review results in changes that protect the integrity of ACCUs, it would make sense for SMCs and ACCUs to become inter-changeable over time.

If market mechanisms are to be used to find the most efficient carbon reduction approaches, the credibility of ACCUs (and SMCs) is paramount.

*Should banking and borrowing arrangements be implemented for Safeguard Mechanism Credits?*

9. Limited banking and borrowing arrangements within a particular Phase should be implemented.

This would increase flexibility and efficiency of emissions reduction and ease the transition to new or emerging technologies. To prevent indefinite borrowing, facilities should be required to bank SMCs before borrowing. As absolute baselines ratchet down over time, the total potential SMCs will decrease. Any banking and borrowing arrangements must consider how the integrity of SMCs from a given year will change over time.

*Should Safeguard facilities no longer be able to generate ACCUs for reducing direct (scope 1) emissions unless they have an existing registered ERF project?*

This should be considered in light of the Chubb review.

*Additional feedback is sought on:*

- *allowing existing ERF projects at Safeguard facilities to continue to generate credits and retaining double counting provisions to prevent a facility from generating ACCUs and SMCs;*

These complexities would be avoided with a simple carbon price, which would allow the market to find the most cost-efficient and effective emission reductions.

This issue should be considered in light of the Chubb review. The mechanism for this will need to ensure that the principle of additionality underpinning ACCUs is not undermined.

- *options for the treatment of deemed surrender;*

10. Deemed surrender should be removed.

Deemed surrender of ACCUs under the Safeguard Mechanism currently allows a facility to receive Government payment for the ACCU as well as reduce its net emissions through the deemed surrender, effectively double counting the reduction.

- *continuing to allow Safeguard facilities to participate in ERF projects that reduce emissions from electricity use (scope 2) emissions;*

This issue should be considered in light of the Chubb review.

- *mechanisms to promote the transparency of the ACCU market, such as publishing unit holding, to assist with market decision making, supply and cost effectiveness.*

This issue should be considered in light of the Chubb review

*Should international units be able to be used for compliance under the Safeguard Mechanism at a future time, noting that any decision would depend on the rules for international trading?*

11. No use of international credits should be permitted until the international market is more developed, with proven high integrity carbon credits

Clear quality control standards are required that are at least as rigorous as Australian standards post-Chubb review. Documented difficulties in ensuring the integrity of international carbon credits would need to be overcome.

## 4. Tailored treatment for emissions-intensive, trade-exposed (EITE) businesses

### 4.1 Defining emissions-intensive, trade-exposed facilities

12. In order to incentivise the required decarbonisation of the economy, exemptions for EITE businesses should be very limited and focused on industries that will be essential in a net zero world.

The consideration of tailored treatments for emissions-intensive, trade-exposed businesses (**EITEs**) is argued to be necessary to ensure carbon-heavy Australian businesses remain internationally competitive and to prevent 'carbon leakage' - the replacement of a carbon-intensive Australian product with an even more carbon-intensive overseas product. Within the context of a national carbon budget and the need to decarbonise the whole economy, it is ineffective, unequitable, inefficient and more complicated to grant special circumstances to EITEs, who are amongst Australia's biggest polluters, under the guise of preserving their operational viability.

The list of eligible EITE activities under the RET includes a range of industrial processes relating to mining, oil and gas and manufacturing, which account for the bulk of facilities covered by the Safeguard Mechanism. A large proportion of current facilities may be eligible for EITE status and therefore exempt from the requirement to reduce emissions.

Any meaningful consideration of EITE industries must consider their potential role in a decarbonised economy and global net zero targets. Some EITE activities produce materials that will be essential in a decarbonised world, only producing emissions as a by-product of current technical processes (e.g. steel or aluminium). Others, such as LNG, will still be producing high levels of Scope 3 emissions even if Scope 1 are brought close to zero and alternatives already exist for their primary uses (renewable energy). The former should be given preference over the latter.

Supporting EITEs through tailored treatment when low or zero carbon alternatives exist (either within or outside the Safeguard Mechanism) is contrary to the objectives of reducing emissions in an equitable and cost-effective way. Allocating EITE industries and facilities additional room in the carbon budget penalises lower carbon alternatives for the progress they have made, as well as increasing the emissions reduction share on facilities that produce for domestic consumption. The growth of green industries for domestic and international markets requires a level playing field that sees the most polluting industries pay for their own emissions reduction. If Australia becomes a renewable energy superpower and exports green energy to current buyers of fossil fuel exports, carbon leakage will not occur and Australian jobs will be retained.

If carbon-intensive industries are not competitive once emissions reduction costs are factored in, then the market is working efficiently to reduce emissions. The contraction and phase out of specific carbon-intensive industries is an expected part of decarbonising the economy and important to reaching our emissions reduction targets. Supporting a just

transition for workers whose livelihoods are connected to EITE industries is crucial to achieving equitable decarbonisation.

In summary, tailored treatment of EITEs should only apply to industries that will be essential in a net zero world but need significant innovation to make a zero carbon alternative viable, and to support a just transition for workers of EITE facilities to green jobs.

*Should a facility-specific comparative impact assessment that builds on existing EITEs definitions be used rather than a sector wide designation?*

For consistency, simplicity, equity, effectiveness and efficiency, any EITE assessment criteria used should be industry wide. Facility-specific impact assessment will give additional special treatment to the most polluting facilities and create incentives for lobbying and unfair differential treatments.

## 4.2 Assistance measures for emissions-intensive, trade-exposed facilities

*Would additional funding opportunities effectively assist EITE facilities to adapt to declining Safeguard baselines?*

13. Additional funding to EITE should be used very sparingly.

Additional funding may assist EITE facilities to reduce emissions and adapt to declining baselines but will reduce the efficiency and equity of decarbonisation efforts both within and outside the Safeguard Mechanism if lower emissions industries do not receive such support.

*What kinds of funding, finance or other arrangements and measures would best support EITE Safeguard facilities to reduce their emissions?*

Additional funding should only be provided to support:

1. a just transition for EITE workers to new green jobs; or
2. R&D and innovation to develop low or zero carbon alternatives to the EITEs. This should be done without penalising green alternatives being developed outside the Safeguard Mechanism.

Additional funding should not be provided to purchase ACCUs for EITEs or to reduce emissions through energy efficiency or with existing technology.

*In particular, what potential design features of the Powering the Regions Fund would support covered facilities with their decarbonisation priorities?*

14. The Powering the Regions Fund should be used at an industry level to support innovation and just transition.

The primary role for the Powering the Regions Fund in supporting EITEs to decarbonise should be to facilitate the transition of EITE industries to new green alternatives, such as green hydrogen and green steel. At the industry level, this could be through investment in R&D and pilot projects. A just transition for workers could be achieved through workforce

development and training in new green technologies, and a jobs guarantee in the emerging industry.

*Is the direct provision of SMCs an appropriate way to mitigate cost impacts for EITE facilities?*

15. EITEs should not be directly provided with SMCs.

Direct provision of SMCs for EITEs does not encourage or facilitate reduction of emissions but gives a free pass to the biggest polluters, reducing effectiveness, equity, and efficiency.

*Are differential decline rates an appropriate way to reduce the impact on EITE facilities?*

16. EITEs should not be given differential decline rates.

Differential decline rates will reduce the burden on the most polluting, reducing equity, effectiveness, and market efficiency.

*How could differential decline rates be structured so that emissions reduction and fairness outcomes are maintained?*

See above.

## 5. Taking account of available and emerging technologies

*Should multi-year monitoring periods be extended to allow facilities with limited near-term abatement opportunities to manage their own abatement path?*

17. Multi-year monitoring periods should not be used as they add unnecessary complexity.

No. If banking and borrowing is permitted, there will already be a mechanism for multi-year variability that can be utilised for adopting new technology. Additional multi-year monitoring periods (**MYMP**) would complicate administrative requirements and reduce progress towards targets. There should be no new MYMP from Phase 1, no extensions of existing MYMP and any existing MYMP should be phased out by Phase 2. If baselines are exceeded, facilities can still buy SMCs or ACCUs.

## 6. Indicative baseline decline rates

*What are the appropriate characteristics for the decline trajectory to 2030 that can deliver the Safeguard Mechanism's share of Australia's climate targets, and the process for setting baselines post-2030?*

18. The decline trajectory to 2030 requires absolute baselines, headroom to be removed and linear decline rates with regular reviews, for all covered facilities.

*Absolute baselines* – Absolute baselines allow a clearer decline path and incentivise growth in green industries, not carbon intensive ones. Intensity-linked baselines could be implemented but emissions could increase due to increased production.



*Removal of headroom* – There will be no decline trajectory if headroom is not removed, as evidenced by previous years.

*Linear decline* - Linear decline of baseline rates will be more effective and more equitable than a ‘soft start’ when actors external to the Safeguard Mechanism are considered. However, linear decline rates become increasingly separate from the Safeguard Mechanism’s share of national emissions over time (see Section 2).

*Regular reviews* - There should be a regular review process to assess whether the 28% share is still appropriate and whether the Safeguard Mechanism as a whole is on target to achieve the required emissions reductions.

*All covered facilities* - EITEs must be subject to the same decline rates as non-EITEs to retain an equitable distribution of costs.

## 7. Other policy issues

### 7.1 Treatment of site-specific production variables

*What transitional or other arrangements should be in place for site-specific production variables, including:*

- *whether the use of Government-defined production variables (prescribed in Schedule 2 of the Safeguard Mechanism Rule) should be mandatory from the start of Phase 1;*
- *whether transitional arrangements for facilities using bespoke, site specific production variables should be considered for Phase 1; and*
- *the proposal that only Schedule 2 production variables could generate Safeguard Mechanism Credits (SMCs)?*

19. Absolute baselines remove significant complexity, including the need to calculate production variables on an ongoing basis.
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### 7.2 Treatment of fixed (schedule 3) production variables

*Should oil refinery production variables:*

- *remain fixed (in Schedule 3) and not generate SMCs; or*
- *become production-adjusted (move to Schedule 2) and be eligible to generate SMCs?*

N/A. Absolute baselines remove the need to calculate production variables on an ongoing basis.

### 7.3 Role of Government-defined production variables

*Are existing Government-defined production variables suitable for the Safeguard Mechanism to drive least cost emissions reductions?*



N/A. Absolute baselines remove the need to calculate production variables on an ongoing basis.

## 7.4 Inherent emissions variability

*Should the inherent emissions variability calculated baseline approach be removed?*

N/A. Absolute baselines remove the need to calculate production variables on an ongoing basis.

## 7.5 Landfills

20. Legacy emissions from landfills should be included at some stage (with an appropriate baseline adjustment), triggering Safeguard Mechanism Credit generation.

The challenges for accounting and crediting landfill facilities stem from the exclusion of legacy emissions in the Safeguard Mechanism. Current baselines only require 37.2% landfill generated gas capture and yet many facilities are already capturing over 70% (and receiving ACCUs for these efforts). For landfills to achieve net zero emissions by 2050, facilities should include legacy emissions at some point before then and be aiming for 100% gas capture. The point at which legacy emissions are included would require a concurrent step change in emissions covered by the Safeguard Mechanism and there would need to be an adjustment to the sector's baseline and the total Safeguard Mechanism cap to reflect this (without changing the non-landfill baselines). Whilst the transition may be awkward, once included, landfills may be able to generate SMCs for trading and the Safeguard Mechanism will be more effective in reducing landfill emissions.

*How should landfills be treated, including:*

- *should landfill baselines decline at the same rate as other facilities;*

Decline rates for landfill baselines will depend on the inclusion of legacy emissions. For example, if this began in Phase 2, landfill baselines could be the same in Phase 1 as other facilities, and then be adjusted for Phase 2 to take into account the new higher baselines.

- *should landfills be able to generate SMCs in Phase 1; and*

Landfills should not be able to generate SMCs in Phase 1 if baselines do not include legacy emissions. Existing ERF projects that generate ACCUs in Phase 1 could continue.

- *should long-term arrangements for landfills be considered prior to Phase 2?*

If considered in advance, long-term arrangement for landfills could be implemented in Phase 2. If this saw the inclusion of legacy emissions in landfill baselines in Phase 2 then landfills would become eligible to generate SMCs. ERF projects that currently generate ACCUs should be transitioned to SMCs to avoid double counting.

## 8. Additional suggestions

### 8.1 Enforcing compliance

21. Options to renegotiate baselines should be removed and penalties imposed on facilities that exceed their baselines.

To ensure the effectiveness of the Safeguard Mechanism, there need to be stronger compliance measures for facilities that exceed their baseline. Currently, facilities that exceed their baseline can apply to renegotiate it in several different ways, prior to any requirements to purchase offsets. Options for adjusting baselines after they have been exceeded should be removed.

If facilities are not eligible for a renegotiated baseline and fail to purchase or generate offsets for excess emissions, the Clean Energy Regulator can impose penalties including infringement notices, legal action, enforceable undertakings (compulsory actions to reduce emissions) or civil penalties up to a maximum of \$18,000 per day. These penalties should be increased substantially to disincentivise baseline breaches, which will become more likely once current headroom is removed.