Emissions Reduction Fund: Safeguard mechanism
Consultation paper
March 2015
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The Government invites written submissions on the Emissions Reduction Fund Safeguard Mechanism Consultation Paper from all interested businesses and members of the community.

Submissions are due by midday AEST, Monday, 27 April 2015. Any submissions received after this date will be considered at the Government’s discretion.

Each submission, unless it is explicitly provided in confidence, will be published on the Department of the Environment’s website. Submissions will remain on the Department’s website. Copyright will reside with the author(s) and not with the Government.

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Where possible, submissions should be sent electronically, preferably in Microsoft Word or other text-based formats, to the email address listed below. Alternatively, submissions may be sent to the postal address below to arrive by midday AEST on the above due date.

All submissions must include a cover sheet, available at www.environment.gov.au.

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            Safeguard Mechanism Branch
            Department of the Environment
            GPO Box 787
            CANBERRA  ACT  2601

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Introduction

The Emissions Reduction Fund is the centrepiece of the Government’s Direct Action Plan to cut emissions to five per cent below 2000 levels by 2020.

It is a $2.55 billion programme to purchase emissions reductions at lowest cost. This will lower our national emissions, while improving the productivity of Australian businesses.

To ensure that emissions reductions purchased through the Emissions Reduction Fund are not displaced by a significant rise in emissions elsewhere in the economy, the Government will implement a safeguard mechanism. This will safeguard the value of funds spent under the Emissions Reduction Fund and create a stable and predictable policy landscape in which businesses can make new investments.

Unlike the carbon tax, the Government will budget no revenue from the application of the safeguard mechanism and businesses will not have any tax liability for their emissions.

The Government has consulted widely on the Emissions Reduction Fund’s design. A Green Paper was released in December 2013 for public comment, followed by a White Paper in April 2014 outlining key design features. Implementation of the crediting and purchasing mechanism is now underway, with the first auction planned for April 2015.

The Government is now working with businesses and the community to implement the safeguard mechanism, the final element of the Emissions Reduction Fund. The Emissions Reduction Fund enabling legislation includes a high-level architecture for the safeguard mechanism, with the policy details to be finalised in legislative rules and in close consultation with businesses. The safeguard mechanism will commence on 1 July 2016, allowing time for this consultation.

The Government made a number of important policy decisions in relation to the safeguard mechanism in the Emissions Reduction Fund White Paper, as outlined below. This consultation paper seeks input from businesses and the broader community on a range of specific implementation aspects of the safeguard mechanism. Once this feedback has been incorporated into the safeguard’s design, the Government will release draft legislative rules for further comment, prior to finalising these rules in late 2015. The timeline for the design and implementation of the safeguard mechanism is illustrated in Figure 1.

Figure 1: Design and implementation timeline for the safeguard mechanism

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The safeguard mechanism is being developed in the context of three design principles established to guide the development of the Emissions Reduction Fund. These are: lowest cost emissions reductions; genuine emissions reductions; and streamlined administration.
For example, to achieve streamlined administration, the Government will primarily rely on existing data and reporting to implement the safeguard mechanism.

In the Emissions Reduction Fund White Paper, released in April 2014, the Government outlined its policy for a number of elements of the safeguard mechanism:

- **Coverage**: the safeguard mechanism will apply to facilities with direct emissions of more than 100,000 tonnes of CO$_2$-e.

- **Baselines**: emissions baselines for existing facilities will reflect the highest level of reported emissions for a facility over the historical period 2009-10 to 2013-14.

- **New investments**: baselines for new facilities and significant expansions will be set at a level to encourage facilities to achieve and maintain best-practice.

- **Compliance**: a flexible approach to compliance will be adopted.

- **Administration**: the safeguard mechanism will be administered by the Clean Energy Regulator.

In November 2014, Parliament amended the *National Greenhouse and Energy Reporting Act 2007* (the Act) to include a high level architecture for the safeguard mechanism, incorporating a number of these and some additional elements, including:

- **Start date**: a 1 July 2016 start date, with rules and regulations in place by 1 October 2015.

- **Coverage**:
  - the safeguard mechanism will apply broadly to a variety of business entities, including corporations, partnerships, trusts, and local councils;
  - the entity with operational control of a covered facility will be responsible for meeting safeguard requirements.

- **Baselines**: the methods for determining baselines, including for new entrants and business expansion, will be set in safeguard rules.

- **Emissions management**: a graduated approach will be applied to encourage operators to comply with their safeguard obligation:
  - a requirement that facility emissions remain below their baselines;
  - a ‘net emissions’ approach, allowing businesses to voluntarily use carbon offsets to net off emissions, as is currently available under voluntary carbon neutral programmes;
  - an exemption for facilities whose emissions are the direct result of exceptional circumstances, such as a natural disaster; and
  - the application of a civil penalty for non-compliance, with an amount to be specified in safeguard regulations.

These design elements are explained in more detail throughout this consultation paper. While the above elements have been legislated, the framework leaves a number of policy questions, such as how to determine baselines for new investments and treatment of the electricity sector, to be finalised. This consultation paper invites feedback on the detailed implementation options being considered by the Government, as discussed in the following sections.
2 Coverage

2.1 Which emissions will be covered?

The safeguard mechanism aims to protect taxpayer funds by ensuring that emissions reductions purchased through the Emissions Reduction Fund are not displaced by a significant rise in emissions elsewhere in the economy. To be effective, it should cover major emissions sources, without imposing unnecessary administrative costs on business.

In response to the Emissions Reduction Fund consultation process, the Government decided that the safeguard mechanism will apply to facilities with direct emissions of more than 100,000 tonnes of CO$_2$-e a year. This threshold will be specified in legislative rules (as per section 22XJ of the Act).

The 100,000 tonne threshold will cover around 140 large businesses—representing around half of Australia’s emissions—from a range of sectors including power generation, mining (coal and metal ores), oil and gas extraction, gas supply, manufacturing (including metals, cement and lime), transport (air, sea, rail and road), heavy and civil engineering construction, and waste.\(^1\) Emissions from the electricity sector represent around 57 per cent of covered emissions. Figure 2 provides a breakdown of covered emissions from the remaining sectors.

Direct (or scope 1) emissions are defined in the Act. They include fuel combustion, emissions from physical and chemical processes and fugitive emissions. Electricity generators will be responsible for the emissions from electricity production.

2.2 Who will participate?

The safeguard mechanism will apply broadly to cover a variety of business entities, including corporations, trusts, and local councils (section 22XH and definition of ‘person’ in the Act). A broad approach reduces the potential for competitiveness issues that could arise if covered and uncovered facilities are operating in the same markets.

The business with operational control of a covered facility will be responsible for meeting safeguard requirements (section 22XH of the Act). This will result in participation by around 140 large businesses that already report under the National Greenhouse and Energy Reporting Scheme.\(^2\)

Placing obligations on the entity with operational control of the facility ensures that responsibility rests with the entity that is best placed to manage the facility’s emissions and take action to reduce them, if needed.

The Joint Petroleum Development Area (JPDA) and Greater Sunrise gas fields will not be covered by the safeguard mechanism (section 6A of the Act). These areas are jointly owned by Australia and East Timor.

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\(^1\) This estimate is based on emissions data reported under the National Greenhouse and Energy Reporting Scheme by corporations and other legal entities in 2013-14 and includes facilities forecast to exceed the threshold in 2014-15.

\(^2\) See Footnote 1.
2.3 What happens if a facility falls below the coverage threshold?

In general, facilities will be covered by the safeguard mechanism while their emissions remain above the coverage threshold. However, a facility that exceeds its baseline and then falls below the coverage threshold will remain covered until the emissions increase has been rectified (refer section 22XF).

2.4 Waste sector coverage

Emissions from landfill facilities consist mainly of the release of methane from decomposing organic material, such as food, paper, garden waste and wood. This organic material decays over time and can release emissions for many years after its disposal. For example, in the first year of the safeguard mechanism, landfill emissions will arise exclusively from waste deposited over previous decades. The landfill operator cannot retrospectively alter landfill composition. This lag between waste disposal and methane generation must be considered in safeguard design.
Consistent with the approach for other sectors, baselines for landfill facilities would be calculated using the highest level of reported total direct emissions over the historical period 2009-10 to 2013-14.

However, given the particular circumstances that apply at landfill facilities, it may not be appropriate to include emissions from waste deposited over previous decades when considering whether a landfill should be covered by the safeguard mechanism or whether it has exceeded its baseline.

One option could be to limit covered emissions in the waste sector to emissions from ‘new’ waste. Under this approach, a landfill would be covered by the safeguard mechanism if emissions from new waste exceed 100 000 tonnes of CO₂-e a year. Covered emissions could then be used to assess a facility’s emissions performance and determine whether it has exceeded its baseline emissions.

New waste could be defined as waste deposited at a landfill after 1 July 2012. Landfill operators were required to take responsibility for emissions from waste deposited after 1 July 2012 under the carbon tax, so could reasonably be expected to manage these emissions for the purposes of the safeguard mechanism.

As noted above, baselines for landfill facilities would be calculated using the highest level of total direct emissions over the historical period 2009-10 to 2013-14. Total direct emissions would include emissions from ‘new’ waste and emissions from waste deposited before 1 July 2012.

Possible approach: Landfill facilities would be covered if emissions from ‘new’ waste deposited after 1 July 2012 exceed 100 000 tonnes of CO₂-e a year. Emissions from ‘new’ waste would also be used to determine whether a landfill facility has exceeded its emissions baseline.

Consistent with other sectors, emissions baselines for landfill facilities would be calculated using the highest level of reported total direct emissions—that is, emissions from all waste, regardless of when it was deposited—over the historical period 2009-10 to 2013-14.
3 Establishing baselines

Baselines represent the reference point against which future emissions performance will be measured. In developing the Emissions Reduction Fund White Paper, the Government decided that emissions baselines will be based on absolute emissions using historical data reported under the National Greenhouse and Energy Reporting Scheme. This avoids introducing new reporting obligations for businesses covered by the safeguard mechanism.

The Government also decided and announced in the White Paper that emissions baselines will be set using the highest level of reported emissions for a facility over the historical period 2009-10 to 2013-14. Using the highest level of emissions over the five year period can help to accommodate natural variability in emissions, for example from changes in production levels, plant maintenance or the types of inputs used. Natural variability was highlighted as a key issue by businesses during Emissions Reduction Fund consultations.

We also support the proposition in the Discussion Paper of using the highest historical emissions point as the initial baseline for each refinery as this will cover the situations that will have arisen during the recent working experience of the refinery and will reduce the need for more detailed discussions and consideration of year on year changes in refinery emissions. (Australian Institute of Petroleum)

The Government is considering several additional implementation options to accommodate both business growth and short-term peaks and troughs in emissions. As outlined in the Emissions Reduction Fund White Paper, the safeguard mechanism will allow baselines to be adjusted to accommodate new investments, including significant expansions (see section 4: New Investments).

In determining historical baselines, three issues may arise for which a policy approach needs to be determined. These issues are discussed below and possible approaches outlined.

3.1 Minimum baseline amount

There may be instances where a facility’s emissions are consistently below 100 000 tonnes CO₂-e between 2009-10 to 2013-14, but increase by enough to trigger the coverage threshold following the commencement of the safeguard mechanism.

To ensure that facilities cannot have a baseline that is lower than the coverage threshold, a minimum baseline of 100 000 tonnes CO₂-e could apply to all facilities.

Possible approach: Emissions baselines will be set using the highest level of reported emissions for a facility over the historical period 2009-10 to 2013-14, with a minimum baseline of 100 000 tonnes CO₂-e for all facilities.

3.2 Changes to facility reporting methods

There may be circumstances that lead a business to change the basis on which facility data is reported. For example, a facility may choose to vary the estimation methods it uses as a basis for reporting emissions. Similarly, some businesses have previously aggregated emissions data across a number of facilities and reported as a single vertically integrated production process. From 2014-15, each facility is required to report its emissions separately.
Whether baselines can be adjusted to reflect changes to emissions reporting depends on the nature of the change.

**Changes to emissions estimation**

For facilities that move to a higher or lower order estimation method, baselines would not be adjusted as it may not always be possible to recalculate or re-estimate emissions over the baseline period. This is because it may not be possible to measure emissions that occurred in the past using a different method.

However, baselines could be adjusted by the Clean Energy Regulator to take account of changes to official global warming potentials (GWPs), which are used to calculate the ‘carbon dioxide equivalent’ emissions for different greenhouse gases. Recalculating baselines would be straightforward as the Clean Energy Regulator has all the required data. Doing so would not require additional reporting.

**Vertically integrated production processes**

Where businesses have previously reported vertically integrated production processes, operators would have the option of ‘filling in the gaps’ to ensure that comparable data is available for previous years over the baseline period of 2009-10 to 2013-14. That is, they could retrospectively report disaggregated, additional or recalculated historical data that is consistent with current reporting for the missing years in the baseline period. However, additional reporting would remain optional.

If a facility chooses not to provide revised historical data, its emissions in the missing years could be determined by the Clean Energy Regulator on a pro-rata basis using disaggregated data reported in 2014-15.

**Changes to facility boundaries**

In cases where a facility boundary has changed during or after the baseline period (2009-10 to 2013-14), reported emissions in the baseline period could be adjusted.

Where separate facilities become one facility, it may be a simple matter for the Clean Energy Regulator to aggregate reported emissions for two or more facilities. Where a single facility becomes multiple facilities, the approach for disaggregation of emissions could be consistent with that proposed for vertically integrated production processes. Operators would have the opportunity to ‘fill in the gaps’ to ensure that comparable data is available during the baseline period. If the facility chooses not to provide revised data, its emissions in the missing years could be determined by the Clean Energy Regulator on a pro-rata basis using the most recent year’s data, if sufficient data is available.

Anti-avoidance measures in the Act will deter businesses from redefining facility boundaries to avoid coverage or to avoid exceeding their baseline.
Possible approach: If there have been changes to global warming potentials, the Clean Energy Regulator could recalculate baselines without requiring any additional reporting.

If a facility’s boundaries have changed, or if it has been reported as part of a vertically integrated production process, operators could have the option to retrospectively report historical data over the baseline period that is consistent with current reporting methods.

If a facility cannot or chooses not to provide revised historical data then baselines will not be recalculated except in the following circumstances:

- if previously reported as a vertically integrated production process, emissions over the baseline period could be determined on a pro-rata basis by the Clean Energy Regulator using the reported 2014-15 disaggregated data;
- if the facility boundary has changed, then emissions for the missing baseline years could be determined by the Clean Energy Regulator on a pro-rata basis using the most recent year’s data.

3.3 Baselines reflecting inherent emissions variability associated with existing natural resources and reserves

As outlined in the Emissions Reduction Fund White Paper, the Government has decided baselines will be established for existing facilities using their highest annual emissions over the baseline period, 2009-10 to 2013-14. Based on further consultation, the Government notes that while such an approach is appropriate for most sectors, there are certain operations for which a historical high point does not fully reflect expected business-as-usual emissions. These are operations where:

- there is a natural resource or reserve associated with the operation of a facility;
- the grade or depth of the resource or reserve will have a direct effect on the emissions performance of a facility;
- the facility has limited ability to control for such emissions; and
- facility emissions are expected to exceed their historical baseline and the change in natural resource grade or depth is the primary reason for this.

Based on these criteria, this will largely apply to a subset of facilities in the mining, oil and gas sectors. The Government is considering allowing facilities that meet these criteria to apply for an adjustment to their baseline using the ‘independent assessment’ approach outlined in section 4.1. This would allow eligible facilities to apply for a baseline that would better reflect future business-as-usual emissions. This approach could be available for the first year of the safeguard mechanism to allow for baseline adjustments while also providing long-term certainty of expected emissions performance.
Possible approach: Businesses could apply to the Clean Energy Regulator in the first year of the safeguard mechanism to adjust their baseline using the ‘independent assessment’ approach if, for that business:

- there is an existing natural resource or reserve associated with the operation of a facility;
- the grade and depth of the resource or reserve will have a direct effect on the emissions performance of a facility;
- the facility has limited ability to control for such emissions; and
- facility emissions are expected to exceed their historical baseline and the change in natural resource grade or depth is the primary reason for this.
4 New investments

The safeguard mechanism will include detailed rules for establishing baselines for new investments and significant expansions that facilitate economic growth and business expansion. This will provide for baselines to be established for new facilities which have not yet commenced operations; and those that commenced recently but do not have sufficient data reported under the National Greenhouse and Energy Reporting Scheme to establish a historical baseline. It will also allow growing businesses to adjust their baselines to accommodate significant expansions in capacity.

As highlighted in the Emissions Reduction Fund White Paper, there is a need to consider the most appropriate approach to setting baselines for new facilities that have already made a final investment decision. These facilities have less scope to change their design than those that have not yet taken a final investment decision. For this reason the Government is considering an approach for facilities that have made a final investment decision that more closely mirrors the approach taken for existing facilities. The Government decided in the Emissions Reduction Fund White Paper that new investments yet to make a final investment decision will be encouraged to achieve and maintain best practice emissions performance.

4.1 New investments already underway

New facilities that have already taken their final investment decisions may have little scope to change their design. Some may have recently commenced operations, but not yet reported under the National Greenhouse and Energy Reporting Scheme. Others may have been operating for some years, but have insufficient data to establish a historical baseline.

This suggests the need for the different treatment of investments that have already committed resources by, for example, taking a final investment decision, commencing construction or having recently commenced production.

The Government is considering that baselines for new investments already underway could be set in a way that reflects the limited scope to change their inherent emissions performance.

Defining ‘investments already underway’

There are many steps involved in planning and developing a major industrial facility, making it potentially difficult to determine at what point a new investment is considered to already be underway. The Government could develop a range of tests to assess whether a business has ‘locked-in’ a particular investment, for example, by asking businesses to demonstrate that a final investment decision has been taken. However, it may be simpler and less costly to apply a universal cut-off date, allowing all investments that first exceed the safeguard coverage threshold before a nominated date to be treated as having made a final investment decision.

Given the significant lead times for developing and undertaking a major investment, the Government is considering a cut-off date of 1 July 2020. This means that new investments—including new facilities and significant expansions—could access the approach for investments already underway, so long as they first exceed the safeguard coverage threshold before 1 July 2020.
Some recently commissioned facilities may already be operational, but have insufficient data reported under the National Greenhouse and Energy Reporting Scheme to establish a historical baseline. The Government is considering whether these facilities could choose to establish their safeguard baseline based on either:

- the approach for investments already underway as outlined below; or
- the highest reported emissions of the limited data set between 2009-10 and 2013-14.

However, facilities that have submitted three reports where emissions are greater than 100 000 tonnes CO₂-e are likely to have completed their ramp-up phase. The Government is considering requiring these facilities to use historical data as a basis for setting their baseline.

Possible approach: New investments—including new facilities and significant expansions—that first exceed the safeguard coverage threshold before 1 July 2020 would have baselines set in a way that accounts for their inherent emissions performance.

Existing facilities that have reported for less than five years could choose the approach for investments already underway (outlined below) or use the highest reported emissions of their limited data set between 2009-10 and 2013-14.

However, where a facility has submitted three annual emissions reports during the baseline period that are over 100 000 tonnes CO₂-e, they must use historical data.

**Baselines for ‘investments already underway’**

The method for setting baselines for investments that are already underway should aim to reflect baseline setting for existing operations, as they have a similar capacity to alter their inherent emissions performance. Baselines could be established by the Clean Energy Regulator on the basis of an ‘independent assessment’ approach, reflecting expected emissions performance. An ‘independent assessment’ approach would be more consistent with the treatment of existing operators. For example, it would take account of individual facility circumstances, as is the case for existing operators through the use of historical baselines. To ensure its integrity, the expected emissions performance would be determined by the Clean Energy Regulator in accordance with legislative rules and assured by a registered independent National Greenhouse and Energy Auditor.

Under an ‘independent assessment’ approach, the Clean Energy Regulator could set baselines reflecting expected emissions performance in the year with the highest level of production over the first three years of operation after emissions first exceed 100 000 tonnes CO₂-e, that is, the year the threshold is exceeded and the following two years. This would be consistent with the treatment of existing facilities and would help to accommodate ramp-up of production during the start-up phase by waiting until the facility had reached the coverage threshold.

In determining the baseline, the Clean Energy Regulator would require the facility operator to provide their expected highest production level during this time and associated emissions intensity, and the resultant expected absolute emissions amount. To further promote transparency, baseline applications under this approach could also be required to include a statement outlining how the operator intends to manage greenhouse gas emissions and energy use at the facility. Where a facility does not successfully apply for a baseline, the Clean Energy Regulator would apply a default baseline of 100 000 tonnes CO₂-e.
Where the estimate differs from publicly available information about expected production levels and emissions performance, the application should justify these differences. Publicly available information may include Environmental Impact Statements or corporate reports for new facilities, and current emissions intensity performance of the facility for significant expansions.

The facility operator would be required to have the emissions estimate assessed by a registered National Greenhouse and Energy auditor to provide the highest possible level of independent assurance of the reliability, accuracy and completeness of the underlying assumptions.

Based on information provided by the facility operator and the independent assessment, the Clean Energy Regulator would determine the baseline in accordance with the legislative rules.

After three years, the baseline could be reviewed against actual performance. If the highest level of actual production over the relevant three year period is different to the forecast, the Clean Energy Regulator could adjust the baseline to reflect the highest actual production level over that period. Where a facility does not provide the required data to adjust the baseline a default baseline of 100,000 tonnes CO$_2$-e could apply.

**Possible approach:** Baselines for new investments that first exceed the coverage threshold before 1 July 2020 could be determined by the Clean Energy Regulator, based on the facility operator’s forecast of emissions in the year with the highest production levels over the first three years of operation after emissions first exceed 100,000 tonnes CO$_2$-e.

An independent auditor could be required to provide assurance over the assumptions underpinning the emissions estimate.

The application could also include a statement outlining how the operator intends to manage greenhouse gas emissions and energy use at the facility.

After three years, a facility’s baseline could be adjusted permanently if the highest level of actual production over the relevant three year period is different from the forecast.

Where a facility does not successfully apply for a baseline, or does not provide the required data to adjust the baseline at the conclusion of the initial three year period, a default baseline of 100,000 tonnes CO$_2$-e could apply.

### 4.2 New investments without a final investment decision

The Emissions Reduction Fund White Paper stated that new investments that have not yet taken a final investment decision will be encouraged to perform at best practice. Encouraging best practice helps to avoid locking in unnecessarily emissions-intensive technologies that could make Australia’s emissions reduction task more difficult in the future.

This section discusses options for establishing baselines for new investments, including:

- defining best practice;
- establishing baselines for new entrants and significant expansions; and
- defining significant expansions.
4.3 Defining best practice

There are two broad approaches to defining best practice internationally. One is technology specific, while the other compares the current performance of industry peers. The latter is generally realised through an output-based metric, such as emissions per unit of output.

A technology approach could involve the development of standards or guidance on the best available technologies for a specific situation. For example, the European Union Industrial Emissions Directive adopts a ‘best available technology’ approach. The European Union engaged numerous experts to establish guidance on what constitutes the best available technology for each industry.

An output-based approach could use existing industry data to form a best practice benchmark against which performance is measured. Where limited data is available, such as for industries that are new to Australia, international best practice data sources could be explored.

The relative advantage of an output-based approach is that it gives businesses greater flexibility about how they manage their emissions. Once the benchmark is established, individual facilities can decide how best to meet it. In contrast, an approach that mandates the use of a particular technology could be overly prescriptive and would rely on government making judgements about best practice technologies for a wide range of industrial processes. Government is not well-placed to make these judgements.

Figure 3: Possible arrangements for new investments

During Emissions Reduction Fund consultations, businesses emphasised that any output-based metric should cater for individual facility circumstances. For example, the emissions performance of a facility that burns coal should not be compared to a facility that uses gas to manufacture the same product. Differences in production processes, fuel type, resource grade and facility location can have a significant impact on emissions performance. However, developing benchmarks can be data-intensive and time consuming. It would also not be feasible to develop benchmarks that reflect the vast array of different circumstances.
Nonetheless, benchmarks could be developed to take account of a limited number of different practices and processes within industries. In addition, benchmarks could be set conservatively, for example, by defining best practice relative to the performance of facilities producing the top (that is, the least emissions-intensive) 10 per cent of Australian industry output, rather than the single best performer. This would provide scope to account for different practices or processes, while maintaining an incentive for businesses to make operational decisions that support less emissions-intensive outcomes.

Possible approach: In general, best practice could be defined as the average emissions intensity of production of the top 10 per cent of Australian industry output and applied to new investments that first exceed the safeguard coverage threshold from 1 July 2020. Where available data is limited, international data could be adapted to determine best practice emissions-intensity.

4.4 Establishing baselines for new facilities and significant expansions at best practice

As discussed above, the Government is considering using a best practice emissions-intensity metric to determine baselines for new investments that first exceed the safeguard coverage threshold after 1 July 2020. The definition of significant expansions is discussed in section 4.5 below.

Under this approach, the facility baseline would be calculated as the aggregate of the baselines for each relevant output at the facility, calculated as:

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\text{Baseline for each relevant output} = \text{Emissions intensity of production benchmark} \times \text{production}
\]

A key question relates to how production should be defined. Using actual production can be problematic for a new investment which may experience a ramp-up phase where production is initially below full capacity. This would likely result in a baseline that is too low, as facilities tend to be less efficient during start up and at times when they are operating below capacity.

To avoid setting unrealistic baselines for investments in their start-up phase, it is proposed that the baseline could be calculated using the highest expected production for the first three years of operation above 100 000 tonnes CO\textsubscript{2}-e, the safeguard coverage threshold. After three years, baselines could be permanently adjusted to reflect the highest actual production over that period.

To streamline administration, a baseline might not need to be developed for outputs that contribute less than 10 per cent of a facility’s emissions, unless requested by the facility operator. Instead, the facility’s baseline could be scaled up using the output that contributes the majority of the facility’s emissions.

In the case of a significant expansion, the best-practice benchmark could be applied only to the new plant or equipment, not the entire facility.
Possible approach: The baseline for new facilities and significant expansions that commence after 1 July 2020 could reflect the highest expected production of the new facility or expansion in the first three years of operation above 100,000 tonnes CO$_2$-e, multiplied by the relevant published best practice emissions intensity benchmark, and aggregated for each relevant output.

Outputs that contribute less than 10 per cent of a facility’s emissions need not contribute to the facility baseline, unless requested by the operator. Instead, the facility’s baseline could be scaled up using the output that contributes the majority of the facility’s emissions.

After three years, baselines could be permanently adjusted to reflect the highest actual production over that period.

4.5 Defining significant expansions

Significant expansions in production leading to increased emissions can be accommodated by increasing businesses’ emissions baselines. However, it would not be efficient to continually adjust baselines in response to routine variations in a facility’s emissions. The design of the safeguard mechanism already includes measures to accommodate natural year-to-year variations in facility emissions, for example by setting baselines based on the highest emissions over a five year period and allowing for multi-year monitoring periods.

A clear definition of ‘significant expansion’ would ensure that baselines are only adjusted when there is a deliberate and sustained increase in business activity. The advantage of relying on a facility operator to show a significant expansion of production capacity is that it is tangible and durable, and is apparent in the installation of new plant or equipment.

There is a need to determine an appropriate expansion threshold. One suggestion is a threshold of 20 per cent. An application to have a baseline adjusted to accommodate a significant expansion would need to be supported by an audit report to provide assurance that the 20 per cent production capacity test has been met.

Once a business can demonstrate that a significant expansion has taken place, the facility baseline could be expanded using the approach for new investments outlined above, by estimating the production and emissions intensity of the entire facility over the independent assessment period. Treating significant expansions and new facilities in the same way helps to maintain competitive neutrality between ‘greenfield’ and ‘brownfield’ investments. Therefore, the new baselines could be set using the ‘independent assessment’ approach for significant expansions that first exceed the safeguard coverage threshold before 1 July 2020, and a best practice benchmark approach for expansions that commence after this date.

Possible approach: Significant expansions could be defined as an increase in production capacity of more than 20 per cent that results from the installation of new plant or equipment.
5 Emissions management

To be effective, the safeguard mechanism must deliver an incentive that is sufficient to deter emissions increases beyond established baselines. But it must do so in a way that does not impose unnecessary costs on Australian businesses.

The Government has clearly stated that the safeguard mechanism is not intended to raise revenue. Unlike the carbon tax, no revenue is anticipated and none has been budgeted.

Businesses have emphasised the need for flexibility in the safeguard arrangements to help them manage their emissions.

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\text{Government should ensure companies have access to a broad range of actions to manage the impact of going beyond the baseline. (Business Council of Australia)}
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\text{Establishing flexible compliance arrangements will be important—in defining the point at which compliance arrangements are triggered, and the multiple compliance pathways available once a threshold trigger has been reached. (Rio Tinto)}
\]

The Government recognises the need to maximise flexibility in safeguard design. The Emissions Reduction Fund legislation has established a high-level framework for businesses to manage their emissions consistent with this principle, including:

- a requirement that facility emissions remain below their baselines;
- a ‘net emissions’ approach, allowing businesses to voluntarily use carbon offsets to net off emissions, as is currently available under voluntary carbon neutral programmes;
- an exemption for facilities whose emissions are the result of exceptional circumstances, such as a natural disaster; and
- a range of discretionary, graduated enforcement options to deter non-compliance, including a final sanction in the form of a civil penalty.

The Government is considering options for implementing this high-level framework. The Government seeks feedback on the detailed options discussed below, and will continue to engage with businesses to ensure implementation of the safeguard mechanism provides affected facilities with workable options for managing their emissions.

5.1 Addressing natural variability of emissions

During consultations on the design of the Emissions Reduction Fund, businesses emphasised that safeguard arrangements should accommodate natural variation in emissions from year to year.

\[
\text{A key consideration to setting baselines is the need to include adjustments for those facilities that experience year to year variability in emissions, most businesses do not operate in a ‘stable state’ but rather are managed to respond to the external environment. There will always be a fluctuation in emissions as a natural part of business... (BP Australia)}
\]

To accommodate this natural variability, the Government is considering multi-year averaging—whereby a facility could exceed its baseline in one year, so long as average emissions over multiple years remain below the baseline—as it gives businesses time to implement emissions reduction projects and is simple to administer.
The concept of multi-year averaging was supported by many businesses during Emissions Reduction Fund consultations.

*This support extends to implementing a multi-year compliance period, where a facility could exceed a safeguard mechanism in one year so long as its average emissions over the full compliance period remain below the safeguard mechanism.*

*(Alinta Energy)*

*...the NFF supports a multi-year compliance period, providing the average emissions over a defined period do not exceed the baseline.* *(National Farmers’ Federation)*

The Emissions Reduction Fund legislation allows for multi-year averaging. Under the legislation, a multi-year monitoring period can be declared by the Clean Energy Regulator, with details—such as the length of the monitoring period and the circumstances in which it would apply—to be specified in legislative rules *(section 22XG of the Act)*.

The Government is considering an approach whereby operators could apply for a multi-year monitoring period where there is a reasonable expectation that a facility’s emissions will exceed its baseline. Applications would be assessed by the Clean Energy Regulator, having regard to:

- whether the operator has previously met all its safeguard requirements; and
- whether the operator has provided satisfactory evidence that the emissions could be returned to baseline levels over an extended period.

If satisfactory evidence is not available, the operator could be given the option to enter into an enforceable undertaking to implement measures to return emissions to baseline levels over the extended period.

The length of the monitoring period should give businesses sufficient time to implement emissions reduction projects, acquire offsets or help capture natural peaks and troughs in emissions. Monitoring period length must also ensure that emissions increases are rectified within a reasonable timeframe.

The safeguard mechanism already addresses year to year variations in emissions during the baseline setting process—with baselines reflecting the highest emissions levels over a five year period. Viewed in this broader context, the Government is considering a maximum monitoring period of three years. The operation of a three year monitoring period is illustrated in Figure 4.
Some businesses also supported an exemption based on an emissions-intensity test, which would allow facility emissions to exceed their baseline, so long as the emissions intensity of production is falling. While an emissions intensity test could be effective in some sectors, many sectors highlighted that rising absolute emissions are often not linked to falling emissions intensity, rendering an emissions-intensity test ineffective at smoothing emissions variations. For example:

*As mining operations mature, mines move from shallow to deep operations, the horizontal and vertical transport requirements increase and the ratio of waste rock to ore increases... For processing operations, intensity can fluctuate with changing ore grades.* (Minerals Council of Australia)

For some sectors, emission intensity approaches can be administratively intense. This is particularly true of sectors where facilities shift products over time, produce many products at the same facility or produce products which are difficult to compare. An emissions intensity test could complicate implementation of the safeguard mechanism while being of only limited benefit.
Possible approach: Operators with emissions above baselines could apply to the Clean Energy Regulator for a multi-year monitoring period of up to three years. This means that the facility could exceed its baseline in one year, so long as its average emissions over the approved monitoring period remain below the baseline.

Applications could outline how emissions will be returned to baseline levels over the monitoring period.

5.2 Net emissions and carbon offsets

A number of businesses currently participate in voluntary carbon neutral programmes and use carbon offsets to net off their emissions. Providing a similar option under the safeguard mechanism provides additional flexibility to business. The ability of facility operators to voluntarily surrender eligible carbon offsets at any time during the safeguard process to remain below baseline levels is provided for under the Emissions Reduction Fund legislation (section 22XK of the Act).

Credits issued under the Emissions Reduction Fund—also known as Australian Carbon Credit Units or ACCUs—will be eligible offsets under the safeguard mechanism (section 22XM of the Act).

Avoiding double counting

The opportunity for businesses covered by the safeguard mechanism to create their own emissions offsets raises the possibility that emissions reductions could be counted twice. This could occur if a safeguard facility is credited for an emissions reduction, then uses the issued credits to further reduce their net emissions under the safeguard mechanism. In this way, each tonne of avoided emissions could be counted twice.

In order to ensure facilities covered by the safeguard mechanism are also able to bid into the Emissions Reduction Fund, the potential double counting issue is addressed. In particular, the Emissions Reduction Fund legislation ensures that emissions reductions are not counted more than once (section 22XK of the Act) by adding Australian Carbon Credit Units issued for abatement at a facility back to that facility’s net emissions. If the facility then uses the Australian Carbon Credit Units as an offset under the safeguard, the facility’s net emissions are correspondingly reduced.

There are two ways that the Australian Carbon Credit Units can be used as offsets to reduce the net emissions at the facility where the abatement occurred.

1. A facility can surrender the units to the Clean Energy Regulator.

2. Alternatively, the units can be sold to the Government under an Emissions Reduction Fund contract. The reduction in the facility’s net emissions occurs regardless of whether the units were sold by the facility itself or by another party. In contrast, if the units were sold to a second facility covered by the safeguard mechanism and that facility then surrendered them to the Clean Energy Regulator, the units would offset the emissions from the facility that surrendered them, not the facility that generated them. This would ensure the units could only be used once.
5.3 Exemptions for exceptional circumstances

During Emissions Reduction Fund consultations, some businesses highlighted the potential risks attached to events beyond their control—such as natural disasters—that could impact on a facility's emissions profile.

The Emissions Reduction Fund legislation provides for legislative rules that would allow the Clean Energy Regulator to disregard emissions increases linked to an exceptional event, such as a natural disaster or criminal activity, and exempt the facility from its safeguard obligation for a defined period of time (see section 22XE of the Act).

To encourage the responsible management of emissions, even under exceptional circumstances the Clean Energy Regulator would be required to consider whether reasonable steps were taken to mitigate the risk of excess emissions arising from the exceptional event, both before and after its occurrence.

The Government is not considering exemptions for events that reflect normal market dynamics or as a mechanism for addressing drivers of emissions variation, such as changes to price, production inputs and outputs, or maintenance.

5.4 Enforcement options

Safeguard requirements must be enforceable to ensure that the mechanism is effective. For this reason, the Clean Energy Regulator has access to a range of graduated enforcement options to encourage operators to comply with their safeguard obligation. These enforcement options are over and above the options for operational flexibility already available to and being considered for operators, specifically:

- a conservative approach to setting baselines (using the historical high point in emissions);
- tailored baselines for new entrants and significant expansions to 2020;
- the ability to adjust baselines for emissions variability associated with natural resources;
- a ‘net emissions’ approach, allowing businesses to voluntarily use carbon offsets to net off emissions;
- the potential for multi-year averaging, allowing a facility to exceed its baseline in one year, so long as average emissions over multiple years remain below the baseline;
- exemptions for facilities whose emissions are the direct result of exceptional circumstances, such as a natural disaster; and
- a sectoral approach to electricity (see section 6).

The available enforcement options have been decided and are legislated. Options available to the Regulator include issuing infringement notices, accepting enforceable undertakings and seeking injunctions to rectify an emissions exceedance. The final sanction is a civil penalty to be imposed by a court, with the maximum amount to be set in regulations. The Regulator has discretion over which enforcement options are most appropriate in circumstances of non-compliance, including whether to pursue court action.
The penalty is designed to encourage compliance, not raise revenue. It is a last resort and will never apply to businesses that meet legislated safeguard requirements. The presence of such a penalty is standard practice in Commonwealth legislation.

Figure 5 presents an overview of the proposed operation of the safeguard mechanism, including scope for a multi-year monitoring period, an exemption for emissions linked to exceptional events and a civil penalty as a final sanction.
**Figure 5: Proposed safeguard mechanism compliance process**

<table>
<thead>
<tr>
<th>STEP 1: REPORTING</th>
<th>STEP 2: NOTIFICATION</th>
<th>STEP 3: APPLICATION FOR MULTI-YEAR MONITORING</th>
<th>STEP 4: MONITORING</th>
<th>STEP 5: FINAL SANCTION</th>
</tr>
</thead>
</table>
| The operator reports facility emissions and may surrender carbon offsets to stay below baseline levels. | The Clean Energy Regulator issues a notice to operators of facilities whose net emissions exceed their baseline in any given year. | The operator can apply for a multi-year monitoring period of a maximum of three years. Any exceedance that is the direct result of exceptional circumstances, such as a natural disaster, will be disregarded. | The Clean Energy Regulator monitors facility emissions over the monitoring period. During this time, the operator can:  
  - Take actions to reduce emissions at the facility; and/or  
  - Offset emissions increases by voluntarily surrendering eligible carbon units. | If a facility’s average emissions over the monitoring period remain above its baseline, the Regulator has the discretion to seek the application of a civil penalty through the court. The operator of the facility has an ongoing obligation to rectify any emissions exceedance. |
6 Electricity sector

The electricity generation sector plays a vital role in Australia’s economic and social prosperity. Reliable and low cost electricity supports the competitiveness of our manufacturing industry and our mining sector, and enables the operation of our essential services. The electricity sector has undergone significant change in recent years and continues to be impacted by a number of technological and macroeconomic factors. Experts within and outside the electricity sector expect electricity generation to play a critical role in providing solutions to current and future emissions reduction challenges by providing a low emissions alternative to liquid fossil fuels used in transport and onsite generation.

Currently, the electricity sector produces around a third of Australia’s emissions and is the single largest source of emissions by sector. While emissions from electricity generation have decreased in recent years due to a range of factors, including a decline in demand and support for renewable energy, the profile of the sector is such that even a small increase in emissions can have significant implications for meeting national emissions targets.

Several businesses in submissions to the Emissions Reduction Fund Green Paper noted the unique characteristics of the electricity sector when compared to other sectors covered by the safeguard mechanism.

_Therefore, as flagged in the Green Paper, the generation and networks sectors could be split out from the rest of the economy in the design of the ERF. The esaa considers that this is a sensible approach given the scale of the electricity industry and the fact it produces a uniform output—megawatt hours—regardless of fuel type or location. (Energy Supply Association of Australia)_

The Government recognises the importance of ensuring that the safeguard mechanism is applied to the electricity generation sector in a way that complements existing energy market objectives.

In the Emissions Reduction Fund White Paper, the Government committed to implementing a safeguard mechanism to encourage businesses to keep emissions within historical baselines. Recognising the significance of the electricity sector to Australia’s emissions, the Government agreed to consult with the sector on the specific application of the safeguard mechanism and its interaction with the Renewable Energy Target.

The Government welcomes stakeholder views on the possible approach to applying the safeguard mechanism to the electricity generation sector outlined in the following section.

6.1 Baselines

Baselines represent the reference point against which future emissions performance will be measured. In the Emissions Reduction Fund White Paper, the Government set out its decision that baselines will be based on absolute emissions using historical data reported under the National Greenhouse and Energy Reporting Scheme. The White Paper also set out that emissions baselines will be set using the highest level of reported emissions for a facility over the historical period 2009-10 to 2013-14.
In response to the Emissions Reduction Fund White Paper and Green Paper, several electricity businesses have suggested that the application of absolute historical baselines on individual generators may lead to perverse outcomes in the electricity sector. In particular, it may lead to low emissions intensity generators choosing not to supply electricity in order to stay below a baseline, resulting in the load being met by potentially higher emission intensity generators.

The electricity sector has also identified that grid-connected generators behave more like a single entity that coordinates production to meet a given level of demand at any point in time. The sector has also noted that in light of the recent decline in electricity demand and the impact of the Renewable Energy Target, emissions from the electricity sector have fallen considerably in recent years.

In light of these features, the Government is exploring the option proposed by the electricity sector of applying a sectoral baseline to the generation sector with individual baselines to apply in the event a sectoral baseline is exceeded (see section 6.3). This is a potential alternative to applying individual baselines in the electricity sector from the commencement of the safeguard mechanism.

**Absolute emissions sectoral baseline**

Under the general safeguard mechanism, the decision to set individual baselines at the high point of historical emissions levels is intended to accommodate variability in emissions at a single facility that may occur over the course of a compliance period due to changes in factors such as production levels.

While a high point of historical emissions is appropriate to accommodate variability at an individual facility, across a sector the variability of individual facilities can be expected to average out. For this reason, under a sectoral baseline, the Government is considering an approach where a sectoral baseline for the electricity sector is set with reference to the average industry-wide generator emissions over a historical period. In light of the recent decline in sector emissions, setting the sectoral baseline in this way would account for expected conditions in the sector while accommodating variability in production levels and any changes in the generation mix over time.

### Possible approach: Establish a sectoral baseline for the grid-connected electricity generation sector based on average emissions over a historical period, as a potential alternative to applying individual baselines in the electricity sector from the commencement of the safeguard mechanism.

#### 6.2 What happens if the sectoral baseline is exceeded?

In the event that a sectoral baseline is exceeded, responsibility for returning the electricity sector to baseline levels needs to be distributed among individual generators. Stakeholders have indicated this should be done on an ex-ante basis and be proportionate to a generator’s contribution to exceeding the safeguard baseline. Options that meet these criteria are limited.

The Government is considering an approach for returning the sector’s emissions to baseline levels that references individual generator baselines. Under this approach, when the sector’s emissions exceeded the sectoral baseline, individual generator baselines would take effect from the following financial year and apply each year thereafter. The sectoral baseline would not be re-established.
This approach would allow individual generators to know their baselines and potential obligations up front, and would apply proportionately to generators’ contributions to exceeding the sectoral baseline by referencing emissions above their individual baselines. A key benefit of this approach is its consistency with the general safeguard mechanism, maintaining overall regulatory and implementation efficiency.

**Individual baseline reference period**

In line with the approach to setting a sectoral baseline, individual baselines would be set with reference to a generator’s average emissions over the same historical period as the sectoral baseline. Individual average baselines would ensure that the sum of individual generator baselines do not exceed the sectoral baseline.

Possible approach: A sectoral baseline could apply to the grid-connected electricity sector until the baseline was exceeded. Individual baselines could apply from the National Greenhouse and Energy Reporting Scheme reporting year following the year the sectoral baseline was exceeded. These individual baselines could be set with reference to a generator’s average emissions over the same historical period as the sectoral baseline.

### 6.3 Electricity sector coverage

The Emissions Reduction Fund White Paper set out the Government’s decision that the safeguard mechanism will apply to facilities with direct emissions of more than 100 000 tonnes of CO$_2$-e a year (see section 2.1). The coverage threshold will be specified in legislative rules (refer to section 22XJ(1)(b) of the Act).

Taking a sectoral approach for the electricity sector also requires consideration of coverage; specifically, which grid-connected generators covered by the sectoral baseline would have an obligation to reduce emissions should a sectoral baseline be exceeded. A threshold of 100 000 tonnes of CO$_2$-e for individual generators, consistent with the general safeguard mechanism, would cover around 99 per cent of emissions across the electricity sector reported under the National Greenhouse and Energy Reporting Scheme. This threshold would maximise coverage while minimising unnecessary compliance costs for generators that do not contribute materially to the sector’s emissions. Off-grid electricity generators not covered by a sectoral baseline could be covered by the general safeguard mechanism if they have emissions of more than 100 000 tonnes a year.

As noted, stakeholders have raised concerns that emissions baselines on low emissions intensity generators may lead to a low emissions intensity generator choosing not to supply electricity in order to stay below its baseline, resulting in the load being met by other potentially higher emission intensity generators.

To avoid the potential for this perverse outcome, coverage could be limited to grid-connected generators whose output is more emissions intensive than the average of the sector, as an alternative to applying baselines to all grid-connected generators.

Possible approach: In the event that the sectoral baseline is exceeded, individual baselines could apply to individual grid-connected generators that emit more than 100 000 tonnes CO$_2$-e and whose output is more emissions intensive than the average of the sector, as an alternative to applying individual baselines to all grid-connected generators.
6.4 Electricity sector emissions management

In the event that the sectoral baseline is exceeded, flexible compliance arrangements would be available to generators that exceed their individual baselines. To ensure consistency, an emissions management framework for electricity could be based on the general emissions management framework for the safeguard mechanism outlined in section 5.

The following outlines the key elements of a possible general safeguard emissions management framework and why they could be appropriate for the generation sector.

Multi-year monitoring period

As for other facilities under the safeguard mechanism, generators could apply to the Clean Energy Regulator to gain access to multi-year monitoring period of up to three years. This would allow a facility to exceed its baseline in one year, so long as average emissions over the monitoring period remain below the baseline. Multi-year averaging can help to accommodate natural variation in emissions from year to year.

Access to offsets and the Emissions Reduction Fund

Consistent with the approach proposed for other facilities under the safeguard mechanism, generators could access eligible emissions offsets if their individual baseline is exceeded. This would include the use of Australian Carbon Credit Units (ACCUs) generated by Emissions Reduction Fund projects. Safeguard participants could also bid for Government funding under the Emissions Reduction Fund to help finance projects that reduce emissions at a safeguard facility.

Exceptional circumstances

As outlined in section 5, provision could be made for the Clean Energy Regulator to disregard emissions increases linked to an exceptional event, such as a natural disaster or criminal act, and exempt the facility from its safeguard obligations for a defined period of time. The Regulator would consider whether reasonable steps were taken to mitigate the risk of excess emissions arising from the exceptional event.

It may also be necessary to accommodate circumstances where an electricity generator exceeds its baseline as a result of being directed to produce electricity by the market operator in response to a significant one-off market event. The Government welcomes feedback on this matter.

Consistent with the general safeguard mechanism, exemptions would not be granted for events that reflect normal market dynamics, such as generator responses to market price signals.

Enforceable obligations

The possible emissions management framework for the general safeguard mechanism provides businesses with a range of options to avoid breaching safeguard requirements. In the event that a facility does not meet its safeguard obligations, the Clean Energy Regulator has access to a range of enforcement options and, as a final step, could apply to the court to have the obligation enforced or seek the application of a civil penalty (see section 5 for more detail). This approach would also apply to covered facilities in the electricity sector.

Possible approach: Apply an emissions management framework that is consistent with the general safeguard mechanism.
6.5 New investments in generation assets

The Government supports a highly productive electricity sector where investments in new assets are made efficiently to meet Australia’s energy needs.

Currently, declining demand and support for renewable energy has contributed to a significant level of excess capacity in the electricity generation sector. Due to these conditions, the Australian Energy Market Operator has found that there would be no requirement to invest in new generation in the National Electricity Market until 2024. A similar investment scenario is predicted by the Independent Market Operator for the South West Interconnected System.

The electricity sector will continue to play a vital role in Australia’s economic and social prosperity. Furthermore, the sector is expected to play an important role in supporting the economy to reduce emissions by providing a low emissions alternative to liquid fossil fuels used in transport and onsite generation.

The general safeguard mechanism will include rules for establishing baselines for new investments and significant expansions. These rules will be designed to encourage new facilities and significant expansions to achieve and maintain best practice, thereby helping to avoid locking in emissions-intensive technologies that could make Australia’s emissions reduction task more difficult.

Given the significance of emissions from the electricity sector and its potential role in providing a low emissions alternative to the use of fossil fuels in transport and industry, the Government considers that it is important that new investments in the sector remain consistent with best practice.

6.6 Defining best practice

Section 4.3 outlines a possible approach under the general safeguard mechanism for using output-based benchmarks. The advantage of this approach over a technology-specific approach is that it gives businesses greater flexibility to manage their emissions without the Government prescribing the use of certain technologies.

In the electricity sector, there are multiple technologies and fuels used to generate electricity. Generation facilities can be located large distances away from end users, including across state boundaries. Ultimately, the product that end users consume is a uniform output—megawatt hours—regardless of fuel type, location or technology used to produce it.

Unlike other sectors of the economy, certain technologies employed to supply electricity currently face constraints in their ability to service all markets. For example, technologies used to meet demand from large industrial facilities for constant and large amounts of baseload power are limited in their ability to respond to spikes in demand from sectors like residential consumers. Such spikes in demand are typically met by generators that can start up with minimal lead times. This implies that it may be appropriate to consider best practice benchmarks in the context of the different types of demand that generators are intended to supply, for example, baseload, intermediate and peak demand.

As outlined in section 4.3 the Government is considering defining best practice under the general safeguard mechanism as the average emissions intensity of production of the top 10 per cent of Australian industry peers.
Section 4.4 outlines a possible approach under which baselines for new investments could be based on a best practice benchmark multiplied by the highest expected production for the first three years of operation to accommodate the ramp up phase. After three years, the baseline could be permanently adjusted to reflect the highest actual production over that period. This approach is intended to apply to the broad range of circumstances faced by new investments across the different industries covered by the safeguard mechanism. The Government considers that this approach could be appropriate for the electricity sector.

**Possible approach:** Apply the safeguard mechanism to new investments in a manner that is consistent with the general safeguard mechanism, and that takes the unique nature and profile of the electricity generation sector into account.

### 6.7 Significant expansions

Section 4.5 discusses treating significant expansions at existing facilities in the same manner as new facilities under the general safeguard mechanism. This is intended to preserve competitive neutrality between ‘greenfield’ and ‘brownfield’ investments.

As outlined in section 4.5, the Government is considering an approach to defining a significant expansion as the installation of new plant or equipment that increases production capacity by more than 20 per cent. This approach could be applied in the electricity sector, where only the installation of new generation units is expected to meet these criteria.

**Possible approach:** Significant expansions could be defined as the installation of new plant or equipment that increases production capacity by more than 20 per cent, consistent with the general safeguard approach.

### 6.8 Arrangements for investment already underway

Section 4.1 sets out an ‘independent assessment’ approach to setting baselines for new investments that are already underway, as businesses that have taken final investment decisions may have little scope to change the design of their project. The Government considers that this approach could be appropriate for the electricity sector.

**Possible approach:** Apply the approach for ‘investments already underway’, as set out under the general safeguard mechanism, to the electricity sector.
7 Administration

Administrative arrangements will be consistent across all elements of the Emissions Reduction Fund.

The Government will make decisions about the design of the safeguard mechanism. Through the Minister for the Environment, the Government will be responsible for making the rules that will guide its operations.

The Clean Energy Regulator will administer the safeguard mechanism and apply its rules, including managing the compliance of covered businesses. In general, determinations and declarations made by the Clean Energy Regulator are subject to review by the Administrative Appeals Tribunal.

The Clean Energy Regulator currently administers the National Greenhouse and Energy Reporting Scheme and has the required expertise to perform the administrative functions associated with the safeguard mechanism.

7.1 Publication of information

To ensure that information about the effectiveness of the safeguard mechanism is available to the public, the Clean Energy Regulator could publish regular information about its operation.

For example, the Clean Energy Regulator could publish the following information each year:

- facilities covered by the safeguard mechanism;
- baseline determinations for each facility;
- baseline applications for new investments;
- covered emissions and surrendered offsets for each facility;
- facilities that have a multi-year monitoring period;
- operators whose emissions over the monitoring period exceed their baseline;
- facilities declared exempt from safeguard obligations due to exceptional circumstances.

7.2 Review

The Emissions Reduction Fund, consisting of the two key elements—crediting and purchasing, and the safeguard mechanism—delivers an enduring framework to help reduce Australia’s emissions, while supporting business growth. In particular, the safeguard mechanism will protect taxpayer funds expended under the Emissions Reduction Fund and provide a stable and predictable framework for businesses to operate within.

The Government is committed to delivering a mechanism that remains effective, efficient and equitable over time. The Government notes that Australia’s emissions reduction task will evolve over time in line with international developments. For this reason the Government considers it appropriate that the mechanism be reviewed on an ongoing basis to ensure that it remains effective.
The Government could undertake a review of the operation of the safeguard mechanism before the end of 2017-18. The review could cover the following elements:

- the operation of the safeguard mechanism in concert with the crediting and purchasing elements of the Emission Reduction Fund;
- the effectiveness of the independent assessment approach for new investments already underway;
- the transition from independent assessment to an output-based approach for new investments;
- any arrangements for existing facilities to adjust baselines;
- the operation of the safeguard mechanism in the electricity sector with reference to the ongoing application of the Renewable Energy Target; and
- the scope and timing of the next review.

As outlined in the Emissions Reduction Fund White Paper, the operational elements of the Emissions Reduction Fund will be reviewed in late 2015. The safeguard mechanism will not form part of this review given the mechanism will commence on 1 July 2016, after the review occurs.

The *National Greenhouse and Energy Reporting Act 2007* (the Act) also includes a legislated review of the Act to take place between 30 June 2016 and 31 December 2018. The proposed review of the safeguard is necessary to consider other Emissions Reduction Fund elements that fall outside the scope of the Act, specifically the crediting and purchasing arrangements of the Emissions Reduction Fund which are enacted through the *Carbon Credits (Carbon Farming Initiative) Act 2011*.

Possible approach: The operation of the safeguard mechanism could be reviewed before the end of 2017-18 to ensure its ongoing effectiveness.