Submissions
Climate Change Authority
GPO Box 787
Canberra ACT 2600
submission@climatechangeauthority.gov.au

AUSTRALIAN ALUMINIUM COUNCIL LTD
Level 1,
18 National Circuit
Barton ACT 2600
Ph: 6267 1800
info@aluminium.org.au

20 May 2020

Dear Mr Archer

Re: 2020 Review of the Emissions Reduction Fund

The Australian Aluminium Council (the Council) represents Australia's bauxite mining, alumina refining and aluminium smelting industries. The Australian aluminium industry has been operating in Australia since 1955, and over the decades has been a significant contributor to the Australian economy. Alongside many decades of economic contribution, the industry is globally comparatively young and well maintained. The industry includes five bauxite mines (>10 Mt per annum), six alumina refineries and four aluminium smelters. Australia is the world's largest producer of bauxite and largest exporter of alumina, and the sixth largest producer of aluminium. The industry directly employs around 14,500 people, including 4,000 full time equivalent contractors. The industry also indirectly supports around 40,000 families in regional Australia.

The Council welcomes the opportunity to provide feedback to the 2020 Review of the Emissions Reduction Fund (ERF), and particularly issues raised in the April 2020 Consultation Paper (the Paper). The Council has focused its submission in response to the specific consultation questions posed in the Paper.

1. *How is the ERF performing overall?*

As represented in the Paper, more than 97% of the abatement contracted to date under the ERF, has been through large-scale vegetation, waste and savanna fire management projects, which are outside the sectors represented by the Council. The Council has therefore had minimal practical contact with the ERF, as there has been limited scope for application of this programme to the industrial sector. The 2019 Expert Panel specifically examined how the ERF could be more successful, in delivering additional abatement through broader application beyond these three dominant sectors. The Council supports broadening of the ERF, in conjunction with other Government programmes, particularly as part of the economic recovery from the COVID-19 pandemic. See also response to Q 10.

2. *What parts of the ERF could be improved and how?*

As outlined in its response to the Expert Panel, the Council believes there are some areas in which the ERF could be improved, which would allow increased application of existing methods to the industrial sector. The Council's members are covered by the Facilities Method, Industrial Electricity and Fuel Efficiency (IEFE) Method, and the Industrial Equipment Upgrade Method. There are technicalities within these methods which the Council sees could be improved including additionality (see response to Q3); crediting period and part facility projects.

Crediting Period

The current crediting period is seven years and under these settings, the Facilities Method is failing to access the potential for additional abatement which could be incentivised in the industrial sector. There is a strong

justification to adjust some, or all, of the current scheme settings to incentivise more abatement from this significant potential source of abatement.

Additionally, current rules only allow a maximum of three ERF contracts over the project period. This is potentially constraining for projects under the Facilities Method as the amount of abatement available each year will be uncertain and full value from a project could potentially be best achieved by contracting more frequently, for example, annually up to seven times.

Scope 2 emission reduction projects under the ERF are given a strong disincentive to pursue projects, due to the current rule which adds Australian Carbon Credit Units (ACCUs) gained from scope 2 improvements to the scope 1 actual emissions of a Safeguard Facility. Emitters operating close to their scope 1 safeguard mechanism baselines must then contract with the Clean Energy Regulator (CER) or be forced to surrender the ACCUs without value to reduce their net emissions number below the baseline.

Part Facility Projects

An impediment to the uptake of the Facility Method is the potential for abatement achieved from a project to be reduced or nullified by background variability in emissions from other parts of the facility. This may include natural process variation, maintenance or external events. This impediment could be addressed by the development of a "sub-facility method" which enabled projects to be carried out with an emissions scope narrower than the whole facility. Such a method would require constraints on defining the project boundary, but many examples exist where rigorous project boundaries could be drawn including use of specific fuels, particular process elements, or the use of the metrics reported under current NGERS arrangements. Facilities will have credible baseline data available (and currently reported) which could be used for projects at a sub-facility level.

In order to use the current Facility Method, the size of the abatement must be very large, and the facility would have to have high confidence that all other process, fuel and emission variables would remain consistent over the life of the project. The main method available for medium sized industrial projects, the IEFE Method has formal statistical and accuracy requirements such as t-statistics, R-squared, relative precision and residuals tests to pass. This IEFE Method requires much more time and a higher technical resourcing requirement than the Facilities Method which is provides a significant administrative barrier to its use.

There may be an interaction occurring between the limited use of an ERF Method, the development of capability to assess it and the development of resources and tools to make the use of the Method more accessible. For example, the persistence model tool in the IEFE Method is still unavailable and requires those using the operating emissions model (sub-method 2) to use default decay factors. The decay factor table in the IEFE Method cuts the project value from 100% in year 1 down to 25% of the abatement value by the 7th year which is significantly lower than would occur in practice. Without a persistence model tool which covers a range of different fuel types and electricity, those using sub-method 2 cannot calculate their own decay factor and are disadvantaged by choosing to use this ERF Method.

3. *Do you have any views on the operation of the offsets integrity standards and the additionality provisions as key principles supporting the integrity of abatement under the ERF?*

The Council believes the additionality provisions are such that they are currently limiting the application of the ERF to potential projects, particularly under the Facilities Method which is a key method for the Council's members. The Facilities Method requires proponents to "categorically conclude the project is driven by the ERF incentive or jointly by the ERF and other factors". This is a result of the narrowly defined offset integrity standards which state "Projects covered by the determination should result in abatement that is unlikely to

occur in the ordinary course of events (i.e. unlikely to occur in the absence of the incentive provided by the scheme)." This is further compounded by a narrow rewording of that into the statement of activity intent.

These constraints are an attempt to develop a standard which can be applied to a wide range of abatement opportunities in the economy and find the appropriate balance between incentivising abatement and ensuring public money is not directed to abatement which is not strictly additional. However, given the amount of greenhouse gas emissions theoretically accessible through the Facilities Method (the industrial sector) and the low uptake of this Method, this suggests the right balance between incentivising abatement and delivering appropriate additionality has not yet been found. The increased uptake in other sectors (such as land sector and waste sector) suggests this balance between these factors has been better incorporated in other methods. Some possible ways to strike a more reasonable approach to additionality, while still maintain offsets integrity, include:

- Align the statement of activity intent more closely with the offset integrity standards within the *Carbon Credits (Carbon Farming Initiative) Act 2011* – for example, require a statement indicating the project was "unlikely to occur in the ordinary course of events";
- Adjust the offset integrity standards to better reflect likely circumstances within industrial operations. A common situation would be for a project to be brought forward in time, increased in scale, or made more certain or a higher priority by the incentive provided by the scheme; none of which are a good fit for the current wording of "unlikely to occur in the absence of the scheme"; or
- Develop parallel initiatives (within or alongside the ERF) which have a requirement and structures more aligned to incentivising additional abatement within large industrial facilities where projects are only likely to attract capital if they deliver on a range of objectives, including commercial objectives. This may require developing more commercial capability as part of the assessment process (as is more typical of engagement with the Clean Energy Finance Corporation (CEFC) or Australian Renewable Energy Agency (ARENA).

4. *Do you think the governance structures of the ERF remain fit for purpose?*

As noted above the Council has only a limited base of experience with the governance structures within the ERF and is not in position to comment on them.

5. *What are your views on method prioritisation, method development and method review processes in the ERF? Please include any thoughts on how these processes could be improved, including how the expertise of industry could be better incorporated.*

The Council's concerns are at this stage, focussed on how the existing methods can be better applied to the industrial sector; rather than on the development of additional methods. However, in principle, the expertise of those within an industry who will develop the projects should be utilised as much as possible, to help optimise the practical application and update of these methods; while still delivering sound abatement opportunities.

6. *What are your views on the suitability of the permanence period discount?*
7. *What are your views on the suitability of the risk of reversal buffer?*
8. *What are your views on the risks posed to land-based abatement and the adequacy of ERF and project-level risk mitigation measures?*
9. *What are your views on the risks to contracted abatement resulting from ERF projects being concentrated geographically and by method type?*

The Council does not have a specific response to these questions, as they are focussed on the land sector.

10. What role could the ERF play in future economic recovery efforts?

The Australian aluminium industry is partially vertically integrated. Around two thirds of the bauxite mined in Australia being used to refine alumina here, and the other third being exported. Of the alumina produced in Australia, about 85% is exported and the balance, smelted to produce primary aluminium. Around 10% of this primary aluminium is then used in Australian downstream manufacturing, with the remainder being exported.

This partially vertically integrated production also uses Australian energy in the forms of electricity, gas and coal; as well as some imported inputs such as diesel fuel, caustic soda and pitch. Further, the value adding to Australia's bauxite resources not only creates an additional $14 billion in export value for the Australian economy, but the domestic conversion also provided the industry some protection against *initial* supply chain shocks from the COVID-19 outbreak.

The longer-term future of the industry will depend on the rate of recovery of the global manufacturing sector and the impact this has on international demand for aluminium. It will also be heavily dependent on Australia's ability to ensure its world class energy resources are translated into internationally competitive, low emissions, reliable energy to ensure industrial production, emissions and jobs are not exported to other countries.

In addition to the changes proposed earlier in this submission, the ERF could have a role in supporting this recovery, in particular in development of a "one stop shop" which could help large industrial abatement projects, which are not a good fit for any individual Government programme (ERF, ARENA, Northern Australia Infrastructure Facility etc). For these large or innovative projects, this "one stop shop" could be beneficial to help provide industry the resources to navigate both existing policy and regulatory mechanisms and with the possibility of amalgamating a hybrid solution of available support for projects. Projects of a more innovative nature are harder to fit to ERF methods and become registered projects, due to the lower certainty of results and abatement. A "one stop shop" proposal for large or innovative projects could be part of the solutions to assist the manufacturing and mining industries in seeking the appropriate pathway for these projects and provide additional pathways as part of the COVID-19 economic recovery.

11. Should the ERF more explicitly address climate resilience and impacts? If so, how?

12. Is there a need for enhanced guidance on how to manage ERF projects for multiple benefits? If so, should this be part of the ERF or complementary programs and policies?

The Council does not have a specific response to these questions.

Given the importance of greenhouse and energy policy to the Aluminium industry, the Council welcomes the opportunity to be involved in ongoing consultation on this matter including engagement with the Climate Change Authority.

Kind regards,

MARGHANITA JOHNSON

EXECUTIVE DIRECTOR
AUSTRALIAN ALUMINIUM COUNCIL
M +61 (0)466 224 636
marghanita.johnson@aluminium.org.au