



20 September 2022

## Response to the Safeguard Mechanism Consultation Paper

The Clean Energy Council (CEC) welcomes the commitment by the Australian Government to strengthen and tighten the Safeguard Mechanism, to provide a robust and predictable framework for Australia's industrial sector to reduce its emissions to net zero by 2050.

The CEC is the peak body for the clean energy industry in Australia. We represent and work with more than 1,000 businesses operating in Australia across renewable energy, energy storage, and renewable hydrogen.

For Australia to reach its goal of -43 per cent by 2030 over 2005 levels, and net zero emissions by 2050, all sectors of the Australian economy and society must participate.

To date, the renewable electricity sector has been doing the heavy lifting, with electricity sector emissions falling by one-fifth since 2016<sup>1</sup>. By contrast, we have seen overall emissions rise from those 215 heavy emitters covered by the Safeguard Mechanism.

These emissions increases make Australian industry vulnerable in a time when the global investment and finance community has signalled its intention to reduce its exposure to carbon-intensive industries. We must urgently lower our industrial emissions and incentivise the adoption of more efficient and greener production processes for Australia to retain, and indeed *grow*, those manufacturing industries which have genuine prospect of making a successful transition to net zero-carbon production.

A strong emissions reduction policy for the industrial sector can also be a catalyst to the development of new net-zero industries, such as green hydrogen, green ammonia and green metals.

This transition is of great strategic importance to the growth of the renewable electricity sector in Australia too. A shrinking industrial sector for Australia will be a handbrake on the clean energy transition, and limit Australia's genuine potential to become a clean energy superpower.

There is therefore much at stake in the Safeguard Mechanism being successfully transformed into an effective framework that can deliver concrete emissions reductions and ultimately net zero manufacturing and production.

To make this happen, excessive emissions allowances currently granted heavy emitters (headroom) need to be removed as soon as possible, baselines reset and then lowered on a

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<sup>1</sup> National Greenhouse Gas Inventory: <https://www.dceew.gov.au/climate-change/publications/national-greenhouse-gas-inventory-quarterly-update-march-2022>

predictable basis in line with our national emissions reduction goals. These emissions reduction goals could (and should) become more ambitious over time, and as such the reform of the scheme must allow for Australian industry to speed up over the course of its net zero journey, informed by the climate science and the advice of the Climate Change Authority.

The CEC supports the guiding principles put forward by the Department of Climate Change, Energy, Environment and Water ('the Department) of *effectiveness, efficiency, equity* and *simplicity*, which should inform the refinement of the scheme.

In the interests of equity and simplicity, we need to minimise special rules and carve-outs for individual or sectoral interests, recognising that all parts of the economy and society must make the transition within a short period of time, and that the world as a whole must make this adjustment. Australia's action is not special, but part of a global effort. Our trade-exposed industries cannot sit out the transition.

While some flexibility may be sensible to smooth the lumpiness of production, emissions and abatement activity by facilities, it should not diminish and distract from the need for speed – we cannot afford to adopt approaches which further delay action, as this will only result in the need for steeper emissions reductions and more costly adjustments for industry at a later date.

The Department's consultation paper raises many issues for stakeholder feedback. In this submission we address the following in the appendix that follows.

1. The industrial sector's share of the abatement task
2. Removal of headroom
3. Fixed versus production-adjusted (emissions intensity) baselines
4. Baselines for existing facilities
5. Treatment of new facilities
6. Treatment of the electricity sector
7. Crediting and trading of Safeguard Mechanism Credits
8. Offsets and their usage (include allowable forms of domestic abatement)
9. Ability for Safeguard Facilities to generate ACCUs
10. Banking and borrowing, and multi-year monitoring periods
11. Treatment of emissions-intensive, trade exposed industries
12. Government support programs

Overall, we welcome the direction of the proposed reforms and many of the proposed refinements put forward in the consultation paper, and look forward to this stakeholder feedback helping to shape the detailed policy proposal and draft rule to be released later this year.

Yours sincerely,



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# APPENDIX

## Clean Energy Council response

### » 1. The industrial sector's share of the abatement task

The CEC supports emissions reduction goals for the Safeguard Mechanism consistent with our national emissions reduction goals of -43 per cent by 2030 and net zero emissions by 2050. In the interests of *effectiveness, efficiency, equity, and simplicity*, the burden for the heavy-emitting industry should match that of the rest of the economy as a whole.

### » 2. The removal of headroom

The CEC supports the removal of all headroom from the commencement of the scheme on 1 July 2023, so as to encourage swift action and create the conditions for crediting and trading to begin from the outset of the reformed scheme.

### » 3. Fixed versus production-adjusted baselines

The CEC supports production-adjusted (emissions intensity) baselines, subject to regular reviews, to allow for rise and fall in emissions based on production, provided that as the paper outlines these are subject to a decline rate and can be 'calibrated to meet any given climate target'.

### » 4. Baselines for existing facilities

The approach to establishing baselines for existing facilities is a crucial design decision, and there are merits and drawbacks to both an industry average benchmark approach and facility-specific emissions intensity baselines. The overriding factor for the government should be to ensure that the baseline settings incentivise *actual* emissions reduction to occur from the outset of the reformed scheme, rather than protect or reward delay.

### » 5. Treatment of new facilities

The consultation paper poses two options for the treatment of new facilities that trigger the Safeguard Mechanism threshold of 100,000 tonnes CO<sub>2</sub>-e after 1 July 2021, being:

1. **Best practice:** calculated as the average emissions intensity of the top 10 per cent of Australian industry performance; or
2. **Industry average:** consistent with the current framework for existing facilities from 1 July 2021.

The CEC considers **both options inadequate**. Most heavy industries in Australia are characterised by only a small number of facilities, meaning that industry averages have little meaning, and that the top 10 per cent of Australian industry performance would represent a small sample size. As an absolute minimum, new plants in Australia should be required to be performing at the **top 10 per cent of global best practice**.

New facilities reaching final investment decisions in the 2020s have the benefit of several decades of climate science, and unambiguous global and now domestic climate policy signalling the need to move to net zero within their lifetimes. Long-life, capital-intensive industrial plants built today must be planning and deploying cutting edge clean technologies which can operate at a fraction of existing plant, if not at net zero.

The appropriate treatment of new facilities is also a question of equity. If new heavy emitting industrial plants come online – such as new gas fields or coal mines – these will increase the speed and scale of emissions cuts required by safeguard facilities overall, making the task harder for existing facilities.

## » 6. Treatment of the electricity sector

As the Department is aware, the electricity sector is subject to a sectoral baseline, which applies collectively to grid-connected generators until it is exceeded. Once the sectoral baseline is exceeded, individual baselines apply to each generator.

The strong levels of investment in large-scale renewable electricity generation capacity mean that the sectoral baseline has never been exceeded and is at no risk of being so. This means that thermal generators have no incentive to participate in the sectoral abatement task by making investments in energy efficiency and other abatement opportunities at their plants.

On the other hand, the continuous growth of renewable electricity generation (supported in part by the Renewable Energy Target and demand for large-scale generation certificates) means that thermal generators are under efficiency pressures which will result in many of them retiring by the end of this decade, and that renewable electricity is very likely to soon supply the overwhelming bulk of power in the National Electricity Market (83 per cent by 2030-31, according to the AEMO Step Change Scenario).

In light of these broader market dynamics afoot, the CEC suggests that the Government should transition to an individual facility basis from 2030, when the Renewable Electricity Target is currently scheduled to conclude. By this time, the share of renewables in the electricity system will be overwhelming, electricity prices should be structurally lower for consumers (due to the much lower reliance on coal- and gas-fired generation) and those emissions-intensive facilities still remaining should not be provided with cover from other sector participants.

## » 7. Crediting and trading of Safeguard Mechanism Credits

The CEC welcomes the proposal for the crediting and trading of Safeguard Mechanism Credits which will support least cost-abatement opportunities to be exploited across the sector. It is important that these credits cannot be traded outside the Safeguard Mechanism.

## » 8. Offsets and their usage

The CEC supports the current position of the Government that the use of offsets should be limited to domestic offsets only, prioritising domestic abatement opportunities in the first instance and supporting the growth and maturity of a domestic carbon credits market. Further down the track – subject to international units meeting stringent integrity criteria and being recognised for compliance with Paris agreements, international carbon credits could play a role as the domestic abatement task grows harder.

The use of offsets should, however, be limited to a modest share of a facility's baselines, so as not to encourage or allow an over-reliance on offsets to meet declining baselines.

The CEC also encourages the Government to consider other forms of domestic abatement (other than Australian Carbon Credit Units) – such as Large-scale Generation Certificates (LGCs) – to be recognised under the scheme as permissible forms of abatement. There is currently strong voluntary corporate demand for LGCs, despite the fact that the Renewable Energy Target has been met, due to the fact that these units are regarded as high-integrity abatement units.

To facilitate the fungibility between the various forms of units, the Government should also consider developing a published and formally recognised exchange rate between LGCs, ACCUs and SMCs. This would improve flexibility and lower compliance cost for facilities and support the renewable sector by placing a floor on LGC prices, particularly post 2030 when mandatory targets for retailers end.

» **9. Ability for Safeguard Facilities to generate ACCUs**

The CEC supports the Government's proposal that safeguard facilities should no longer be permitted to accredit new ACCU projects, on the basis that there is a legislated obligation for heavy emitters to make substantial reductions to their emissions.

» **10. Banking and borrowing, and multi-year monitoring periods**

Providing some limited flexibility to industry to smooth its uneven emissions profiles and cost allocations over short timeframes (eg. 1-2 years) has merit. However, we note that the crediting and trading opportunities associated with Safeguard Mechanism Credits, should be able to provide some of this flexibility.

In addition, it is important that additional flexibility via banking and borrowing allowances do not result in facilities delaying actions to reduce emissions. Our position is therefore that any banking and borrowing permissible within the framework would need to be constrained to relatively short windows of time.

With these flexibility features of the incoming framework – crediting and trading, and banking and borrowing – the CEC considers that multi-year monitoring periods become unnecessary, and can be phased out.

» **11. Treatment of emissions-intensive, trade exposed industries**

Public policy to support emissions-intensive, trade-exposed industries/facilities (EITEs) should be directed at addressing a loss of competitiveness by trade exposed industries to other international markets due to the uneven application of climate policies, rather than to shield them from the need to play their part in emissions reduction activities.

To this end, we note that momentum on global emissions reductions and clean manufacturing has accelerated since the Safeguard Mechanism came into operation in 2016, and many of our trading partners are implementing strong policies to drive a transition to cleaner production.

It will therefore be important for DCCEEW to undertake regular assessments of emissions reduction policies being applied across our key trading partners to ensure that policy support is carefully calibrated to genuine competitive risks, and that EITEs are not being unnecessarily compensated for disparities which do not exist.

Further, responsible EITEs policy must also seek to address the converse risk that weak climate policy will expose Australia to declining competitiveness as international producers move faster towards clean technologies and production processes.

» **12. Government support programs for EITEs**

The Department considers a range of support options to minimise adverse cost impacts on emissions-intensive trade-exposed facilities, including grant programs through the Powering the Regions fund, the direct provision of Safeguard Mechanism Credits, and differential decline rates for baselines (ie. a slower decline).

The CEC does not support the gifting of credits or differential decline rates which effectively provide EITEs with abatement exemptions. Any support programs should be squarely aimed at accelerating the carbon competitiveness of Australian industry, rather than removing incentives for facilities to pursue abatement activities. As such, the CEC supports the use of the Powering the Regions Fund, as well as ARENA and CEFC to support industrial decarbonisation projects that align with their established investment goals.

In terms of broader policy frameworks that can assist Australian industry to develop its own clean industries, the CEC would also encourage the Australian Government to closely consider the proposal

from the Grattan Institute (see [The Next Industrial Revolution report, June 2022](#)) for the development of a national embodied carbon accounting methodology and scheme (leveraging NGERs). Such a scheme (which would be complemented by national/state/territory policies for government procurement of low-carbon/green commodities (iron, steel, aluminium etc)) would create a reporting framework that would assist industry to consistently track and report embodied carbon emissions within their supply chains, and ultimately earn a price premium for lower-carbon materials.

We note that the new *Inflation Reduction Act* in the United States, which will direct US\$369 billion to energy and climate related programs, [has committed the US Government to prioritise the purchase of steel, concrete, asphalt and flat glass that have lower levels of emissions](#). The establishment of a greenhouse gas emissions transparency scheme for supply chains will support these procurement goals.

Support schemes of this kind can assist industry to build new markets for low-emissions products, and a national scheme – with the participation of the federal, state and territory governments – should be considered for Australia.