

THE CARBON POLLUTION REDUCTION SCHEME AND THE ROLE OF VOLUNTARY EMISSIONS REDUCTION

PURPOSE OF THIS MAV MEMBERS BRIEF

On the 15 December 2008 the Australian Government released its White Paper on a national carbon pollution reduction scheme, as the centrepiece of the government's strategy for addressing climate change.

The White Paper sets out the Government's policy in relation to:

- a medium-term target range for national emissions reduction
- the design of the Carbon Pollution Reduction Scheme

The Carbon Pollution Reduction Scheme (CPRS) will make industries for the first time, take the cost of carbon pollution into account in their investment and production decisions, and pay for the carbon pollution they generate. This will affect the pattern of competitiveness across the economy, the relative price of goods and services, and the consumption choices made by households and businesses.

(For further information on the CPRS see MAV Members Brief Whitepaper on the Federal Carbon Pollution Reduction Scheme www.mav.asn.au).

On 31 December 2008 the Australian Government released a further paper, the National Carbon Offset Standard Discussion Paper. The discussion paper is concerned with voluntary activity that occurs beyond that imposed by the mandatory compliance market.

The purpose of this brief is to inform MAV member councils of the implications of the CPRS on voluntary emissions reduction activity and on the concept of 'carbon neutrality'.

INTRODUCTION

The introduction of a national Carbon Pollution Reduction Scheme (CPRS) will restrict the quantity of greenhouse gas emissions from sources covered by the scheme. In effect the CPRS acts as a 'cap' above which the aggregate quantity of emissions, from these sources, cannot rise. The cap is imposed to achieve the Government's announced emissions reduction target of 5-15 per cent by 2020 below 2000 levels.

In the absence of the scheme, many companies and individuals, including councils, have undertaken voluntary action to reduce or offset emissions arising from their operations. This action has largely been in the form of purchase of carbon offsets, energy efficiency activities and the purchase of GreenPower™.

The CPRS is a market based response to climate change. After the CPRS is introduced on 1 July 2010, voluntary action will continue to have a role to play in this new operating environment. However, the outcomes of voluntary action will change in certain cases and it is likely that new offset products will be developed while others disappear. The reason why an individual or council chooses to undertake a specific form of voluntary action needs to be carefully considered in the context of the CPRS and the benefits of each form of action understood.

VOLUNTARY ACTION – BEFORE AND AFTER THE INTRODUCTION OF THE CPRS

In the absence of the CPRS, voluntary action, such as the purchase of carbon offsets, GreenPower™ or consumption of less emissions-intensive fuels, led to a direct reduction of emissions at the company / household (i.e. the 'entity') level and in the quantity of greenhouse gases emitted to the atmosphere (i.e. the 'aggregate quantity of emissions').

With the introduction of the CPRS, voluntary action will continue to reduce emissions at the entity level. Individual action will also contribute to nation-wide efforts to achieve Australia's 5-15 per cent emissions reduction target. However, many forms of voluntary action will no longer achieve emissions reductions beyond this target.

If an activity is in a sector covered by the scheme, such as electricity or fuel, the contribution of that activity to a reduction in greenhouse gases changes. The CPRS effectively introduces a 'floor' below which emissions reductions in scheme covered sectors cannot fall.

For example, when a council purchases GreenPower™, the electricity generator, who is liable to purchase CPRS permits for the emissions from the electricity it supplies to consumers, will not require as many permits, as the demand on its generation and therefore permits is lessened. This in turn frees up permits for purchase by other liable companies. As previously stated, the level of emissions and in turn corresponding number of permits in the Australian carbon market place is capped. Therefore, permits will be bought and sold in the carbon market by companies to meet their CPRS obligations, and to ensure Australia is on track to meet its emissions reduction target. Voluntary action that reduces demand for permits by one entity enables the freed-up permits to move to another entity, but this action will not achieve emissions reduction outside of this 'cycle' of permit activity, i.e. beyond the national emissions reduction target.

WHY THE CARBON POLLUTION REDUCTION SCHEME IF IT AFFECTS THE ACHIEVEMENTS FROM VOLUNTARY ACTION?

Addressing climate change is an enormous global challenge. Australians have long undertaken activity to reduce their greenhouse gas emissions. This has occurred largely in the absence of a national regulatory framework. However, the concentration of atmospheric greenhouse gases continues to rise, rather than reduce, and it has come to be widely recognised that voluntary action will not achieve the

scale of emissions reduction required to give the global community an opportunity to avoid triggering 'dangerous climate change'¹.

In response to community demand for concerted and significant action, the Australian Government has developed the national Carbon Pollution Reduction Scheme. Whilst, there is debate and concern that the emissions reduction target set by the Australian Government is scientifically inadequate, economic theory would suggest that the creation of a carbon market will provide a strong financial incentive for companies to reduce their emissions. Continuing with business as usual will cost more than it has in the past; reducing emissions will lessen the exposure to a carbon price. A carbon market, whose integrity and achievements are ensured with regulatory oversight, will achieve more than voluntary action alone. That said the next challenge for the Australian Government and community will be creating a synergy between the carbon market and continued voluntary action.

ARE VOLUNTARY EMISSIONS REDUCTION ACTIVITIES STILL WORTHWHILE?

Since the release of the National Voluntary Offset Standard Discussion Paper much debate has ensued about the value of voluntary emissions reduction after the CPRS commences. Questions have been raised as to why one would continue to spend effort and money when many past (and popular) forms of action will no longer provide an environmental benefit beyond what the Australian Government has committed to achieve anyway with its 5-15 per cent target. Comments have been made that voluntary activity by households and communities also reduces the 'cost to polluters'.

The MAV contends that there is value in continued voluntary emissions reduction activity by councils and community, but councils must understand the specific achievements of each form of action and make well informed decisions about the associated allocation of resources.

In the three sections that follow, the MAV offers an analysis of the 'pros and cons' of continued energy efficiency, purchase of GreenPower™ and purchase of voluntary offsets such as those offered by the Australian Government accredited GreenHouse Friendly™ program. The MAV leaves it to each council to form its own judgment as to which voluntary emissions reduction activity it would choose to utilise after the CPRS is introduced. A brief comment is also offered on the additional opportunities for voluntary emissions reduction.

The MAV concludes this Members Brief with an analysis of the implications for councils of the CPRS on the concept of 'carbon neutrality'.

¹ The term 'dangerous climate change' is commonly associated with an average global warming of 2⁰C over pre-industrial levels. The Garnaut Climate Change Review states that a stabilisation target of atmospheric carbon-dioxide equivalent (CO₂-e) concentration of 450 parts per million gives a 50 per cent chance of exceeding this warming level.

ARE ENERGY EFFICIENCY ACTIVITIES STILL WORTHWHILE?

For many years councils and community have chosen to improve the energy efficiency of their operations. A range of drivers have led to this action; prevalent has been the motivation to do something 'good for the environment'.

With the introduction of a carbon market, actions to improve energy efficiency will no longer have a direct environmental benefit beyond that which would have been achieved anyway by the national emissions reduction target (as explained on p.2).

Despite the absence of an environmental gain, there are still positive reasons why energy efficiency should continue.

Where a consumer has a demand for emissions-intensive energy, the consumer can expect to bear the cost of the associated emissions, passed through the supply chain from the entity liable to purchase carbon permits (for example, the passed through cost from the electricity generator). Reduced consumption of emissions-intensive energy, as achieved through improved energy efficiency, will in turn reduce the exposure of a household or business to the cost of the Carbon Pollution Reduction Scheme.

Further, when a consumer reduces their energy needs, there will be a subsequent decline in their electricity bill, the demand for electricity to be generated, emissions from the electricity sector and therefore the demand for permits. This will in turn reduce the carbon price and the cost to the Australian economy of achieving progress toward the national emissions reduction target. As the cost to the economy decreases it becomes increasingly feasible to set more ambitious emissions reduction targets.

In summary, energy efficiency leads to a financial benefit for the individual, through reduced exposure to the carbon price. Further, the reduced cost to the national economy of operating the CPRS may provide the Australian Government with the mandate it seeks to set a more ambitious emissions reduction target.

IS THE PURCHASE OF GREENPOWER™ STILL WORTHWHILE?

The rationale for the continued purchase of GreenPower™ by households and businesses is much like the rationale for improving energy efficiency. Whilst, in the new carbon market, the purchase of GreenPower™ will no longer have a direct environmental benefit beyond that which would have been achieved anyway by the national emissions reduction target, it none-the-less offers positive outcomes.

The purchase of GreenPower™ sends a market signal that emissions-intensive goods and services are not desirable. Consequently, these market signals should stimulate demand for the accelerated supply of less emissions-intensive energy sources. With demonstrated demand and increased supply, the cost of these improved forms of energy can over time expect to be lower than the emissions-intensive alternative. Further, if GreenPower™ continues in much its current form it will create this demand as additional to what the national Renewable Energy Target will achieve.

It should be noted that for the period that the CPRS permit price is low (proposed at \$25/t CO₂-e at scheme introduction), it can be expected there will remain a price premium on GreenPower™. Over time, as scarcity in the carbon market is introduced and the permit price rises, the pricing gap between GreenPower™ and emissions-intensive energy will narrow and eventually reverse.

By contributing to the accelerated supply of less emissions-intensive goods and services, the purchase of GreenPower™ will assist the creation of 'green collar' industries across Australia. These industries will stimulate local economic activity and create employment opportunities.

WILL VOLUNTARY OFFSETS STILL BE AVAILABLE?

The nature of the voluntary offsets available within Australia will change substantially upon commencement of the CPRS.

Offsets that have in the past been accredited under the Australian Government's GreenHouse Friendly™ program have been required to satisfy a number of criteria. An offset must demonstrate additionality, permanency, measurability and transparency, amongst other criteria.

The core criterion to consider in the context of the CPRS is that of additionality. This means that the greenhouse gas abatement achieved must be beyond what would be undertaken as part of business-as-usual investment or beyond what is required by regulation. In this regard offsets that offer abatement from a sector covered by the CPRS will most likely fail to satisfy the criteria for additionality, because Australia would have achieved it anyway by having in place an emissions cap.

Consequently the pool of available domestic offsets will diminish significantly, as they can only be generated from sources not covered by the CPRS. The Australian Government has signalled its intention of commencing a phase-out of the GreenHouse Friendly™ program and dissolution come 1 July 2010².

Recognising that a core motivation for individuals, businesses and councils to purchase offsets has been to reduce the environmental impact of their activity by paying for a greenhouse gas emissions reduction elsewhere, it can be expected that the demand for products and services that continue to offer abatement will remain.

In the way that the voluntary offsets market emerged over the past decade in response to community and corporate demand, so too can it be expected that a market will emerge for new products and services that offer a means of achieving an environmental gain beyond that which the CPRS will achieve. It will be critical that the Australian Government and its regulators ensure the integrity of the market as it does emerge.

² This has not been formally announced by the Australian Government but has been publically stated by a government senior representative.

Possible sources of future domestic offsets that demonstrate additionality, permanency, measurability and transparency, may include forest management (plantation forests established before 1990 and all native forests on managed land that are maintained as forested land until 2012), revegetation (establishment of woody biomass that does not meet forest criteria), agriculture and soils, and waste (emissions from landfill sites closed prior to 30 June 2008). To the extent that entities responsible for uncovered emissions sources are acting in anticipation of future coverage (e.g. agriculture), or as part of an obligation to contribute to abatement effort, there may be difficulty proving additionality.

The Australian Government is proposing the development of an Australian standard to identify what constitutes a robust, permanent and verifiable carbon offset. This standard should provide consumer confidence in the offset products available in much the same way that GreenHouse Friendly™ has to date.

Beyond the domestic offsets market, there will be opportunities for purchase of international offsets, provided they are not similarly covered by a cap and trade scheme elsewhere in the world.

WHAT OPTIONS EXIST TO DO MORE?

For an Australian community raised to feel a moral obligation to 'do their bit' for the environment, the CPRS may feel disempowering. As such, new opportunities for individual action must be developed and understood.

Within the confines of the CPRS the opportunity does exist to take voluntary action that goes beyond the 5-15 per cent national emissions reduction target. The primary mechanism is to purchase and 'retire' carbon permits.

Any individual, business or council can choose to participate in the national carbon market. The CPRS White Paper states that "a permit could be held and traded by any legal or natural person" regardless of whether they have any legal obligations under the scheme.

Where a council might for instance, decide that it no longer wants to commit its resources to the purchase of voluntary carbon offsets or GreenPower™ it may instead choose to purchase and retire carbon permits. This means that it buys permits at the going market rate and requests that the permit is struck off or retired from the national permit register, so that it can never again be traded. This action achieves several outcomes.

If an individual or council undertakes voluntary action by purchasing and retiring carbon permits, the supply of permits in the national carbon market tightens, creating scarcity and driving up the carbon price. Consequently, the price of emissions-intensive goods and services rise and low emissions alternatives become more competitive.

In terms of emissions abatement beyond the CPRS, the Australian Government has committed to not count any retired permits, or other Kyoto Units, toward the attainment of the national obligations under the Kyoto Protocol. This means, that the purchase and retirement of permits is additional abatement above the 5-15 per cent national emissions reduction to be achieved by 2020.

Beyond the purchase and retirement of domestic carbon permits, individuals, businesses and councils may choose to purchase and surrender a range of international Kyoto units. These units, called Certified Emissions Reductions Units, are generated through initiatives such as the Clean Development Mechanism or Joint Implementation projects. Retirement of international units would offer the same benefits as retirement of domestic carbon units. A council may choose to look to international units where a preference is expressed for one form of abatement over another, e.g. to support abatement in developing countries.

Beyond the carbon market place, councils and communities may also choose to advocate for a more ambitious national emissions reduction target. The Australian Government has stated that it set the target at 5-15 per cent below 2000 levels by 2020, as this was 'responsible leadership in the context of the global financial crisis'³. The Prime Minister has further indicated that he would seek a mandate from the people of Australia for a more ambitious emissions reduction target, and that he accepts the findings of the Garnaut Climate Change Review that it is in Australia's best interest to progress toward emissions reduction to 450ppm CO₂-e by mid-century.

WHAT WILL THE CPRS MEAN FOR THE CONCEPT OF 'CARBON NEUTRALITY'?

In recent years a number of Victorian municipal councils have resolved to become carbon neutral by a date into the future.

The claim of 'carbon neutrality' indicates that an individual entity (e.g. council) has not added to the quantity of emissions in the atmosphere. For example, a council has calculated its annual greenhouse gas emissions (carbon footprint) and taken action to fully offset these emissions; consequently there is no net change in the stock of greenhouse gases in the atmosphere.

With the introduction of the CPRS, industries will be required to pay for their greenhouse gas emissions. It is expected that the full cost of CPRS compliance will be passed through to the consumer.

For councils who own and operate facilities, such as landfills that trigger a CPRS annual emissions threshold, they will be required to purchase carbon permits. Councils as consumers will also be exposed to the carbon price.

In considering how a council can achieve 'carbon neutrality' in the new CPRS environment, purchasing carbon permits to comply with mandatory scheme requirements is not sufficient to then claim carbon neutrality.

Instead, a council must ensure they meet their compliance responsibilities, and then take additional voluntary action to fully offset their emissions.

For a council or business to fully offset their emissions there will be a significant increase in the cost of claiming their operations, a product or service are 'carbon neutral'. Once the CPRS is introduced, under

³ The Prime Minister, Kevin Rudd, statement made during National Press Club Address 15 December 2008.

this approach, liable entities will need to meet the cost of purchasing offsets equivalent to the calculated footprint in addition to the cost of scheme compliance.

All claims of 'carbon neutrality' will be subject to the oversight and penalty from the Australian Competition and Consumer Commission (ACCC).

Where a council or business does not have scheme obligations, and seeks to become carbon neutral they will incur the cost of voluntary offsets plus pay for the passed through carbon price as a consumer.

Having to meet the financial cost of the CPRS and the cost of offsets is likely to reduce the appetite for undertaking voluntary action and for resolutions of carbon neutrality.

CONCLUSION

The purpose of this brief is to inform MAV member councils of the implications of the CPRS on voluntary emissions reduction activity and on the concept of 'carbon neutrality'. It has provided an analysis of the opportunities for continued voluntary action by councils, businesses and community, and for each option provided comment on the outcomes achieved.

The MAV does not seek to suggest any one form of action is favourable over another. Rather, the MAV leaves it to each council to determine what outcomes they seek through voluntary action and in turn match these with the opportunities for action.

The final voluntary carbon offset standard is to be delivered by the Australian Government by mid-year.

For a copy of the National Offset Standard Discussion Paper visit www.climatechange.vic.gov.au

Submissions on the discussion paper can be made until 27 February 2009. The MAV will be making a submission and asks councils to contact the MAV to inform us of council views. The MAV also encourages councils to make a submission.

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Disclaimer

The Municipal Association of Victoria (MAV), in providing this brief to member councils, offers an interpretation of the implications of the national Carbon Pollution Reduction Scheme for local government voluntary emissions reduction actions. The MAV cannot be confident that this brief is without error and as such does not take responsibility for any future action or outcome arising based on the information contained herein.