

A guide to the frameworks supporting Australian Carbon Credit Units and the domestic carbon market



Overview

The Emissions Reduction Fund (ERF) has provided the overarching framework for Australia's carbon markets since 2015, when it was established as the successor to the Carbon Pricing Mechanism (CPM).

The ERF sought to incentivise emissions reduction and avoidance activities across the Australian economy through three key elements: crediting, purchasing and safeguarding emissions reductions.

The scheme has been overseen by the Clean Energy Regulator (CER), the government body responsible for administering legislation for reducing greenhouse gas emissions and increasing clean energy use.

Following a change of government after the May 2022 federal election, the incoming Labor Government is transitioning Australia's carbon crediting framework away from the approach set out under the previous ERF, and is now implementing the climate policy suite outlined in its 'Powering Australia' plan.

Crediting Emissions Reductions

ERF methods and projects

The ERF has allowed organisations and individuals that adopt new practices and technologies that reduce their emissions to generate and sell Australian Carbon Credit Units (ACCUs).

The scheme has overseen a range of emissions reduction and avoidance activities. To earn ACCUs, organisations and individuals implemented these activities in accordance with project guidelines and rules known as methodology determinations, or methods.

Methods set out how a particular activity or project type must be undertaken, how emissions reductions are calculated, and the monitoring and reporting requirements for creating an ACCU.

One ACCU is generated for every tonne of carbon dioxide equivalent (tCO₂-e) calculated to have been avoided or removed from the atmosphere.

Approved ERF methods fall under the following project types:

- Vegetation
- Landfill and waste
- Agriculture
- Savanna burning
- Energy efficiency
- Industrial fugitives
- Transport
- Facilities

Purchasing Emissions Reductions

The ERF Auction

When the ERF was established, the Federal Government allocated \$2.55 billion to purchase ACCUs through reverse auctions. These funds were topped up with an additional \$2 billion assigned to the ERF through the Climate Solutions Fund (CSF), available from 2020.

Under the ERF, taxpayer-funded auctions have historically been the central policy lever driving emissions reductions to help Australia achieve its climate targets, with the Federal Government the primary purchaser of ACCUs.

During this time, ERF auctions have been announced in advance by the CER and held twice annually, over a two-day period. Participants in the auction had to register their project(s) and be qualified for the specific auction, allowing them to bid.

Successful participants immediately entered into a Carbon Abatement Contract (CAC) with the CER to deliver ACCUs to the Federal Government at the price bid at auction.

All the details regarding contract requirements, such as length, delivery schedule, abatement volume and price were established and agreed to between the participant and the Federal Government as part of the auction registration, qualification and bidding components.

Until recently these were "fixed" contracts requiring delivery to the CER. The last auction was entirely of "optional" contracts allowing sale to other buyers, should better prices be on offer.

In March 2022, the Morrison Government enabled a staged process whereby participants with fixed delivery requirements can sell previously contracted ACCUs to private entities with the payment of an exit fee.

Although the Federal Government has been the primary buyer of ACCUs historically, credits are also sold to private entities.

Although the Federal Government has been the primary buyer of ACCUs historically, credits are increasingly being sold to private entities. For example, companies might purchase ACCUs to fulfil some or all of their requirements under voluntary carbon neutral commitments, such as the Australian Government's Climate Active program.

A second driver of private sector demand for ACCUs alongside voluntary buyers is the compliance market, which includes entities with obligations under the Safeguard Mechanism.

The Safeguard Mechanism

From safeguarding Australia's emissions reductions to driving industrial decarbonisation

The third component of the ERF has been the Safeguard Mechanism, which was initially established to ensure that emissions reductions achieved by the ERF's crediting and purchasing incentives were not displaced by rising emissions elsewhere in the economy. The Safeguard Mechanism covers the industrial sector, which is comprised of large businesses with annual emissions exceeding 100,000 tCO₂-e.

These facilities must keep their emissions below a calculated baseline set by the CER. Facilities who exceed their baseline can remain compliant under the mechanism by purchasing and surrendering ACCUs.

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Next steps for ACCUs and the Australian carbon markets

Improving integrity and driving the net zero transition

Following the change of government, the Albanese Government announced its intention to transition the Safeguard Mechanism to a baseline and credit scheme.

Under this approach, emissions limits prescribed to facilities under the mechanism will begin gradually declining, commensurate with Australia's 2050 net-zero target.

To inform these changes the Department of Climate Change, the Environment, Energy and Water (DCEEW) will hold public consultation with industry and the community.

These changes to the Safeguard Mechanism will be implemented from July 2023, from which point the primary driver of ACCU demand will begin graduating from taxpayer-funded purchases through ERF auctions to the compliance market, made up of large industrial emitters with obligations to keep their emissions below declining baselines.

The Federal Government has stated its intention to continue funding ACCU purchases on behalf of the Commonwealth through the newly established Powering the Regions Fund (PRF). The PRF is being established with remaining uncommitted funds from the ERF and CSF.

It is yet unclear what proportion of these funds will be committed to purchasing ACCUs versus the additional purposes outlined in the PRF's expanded remit, which is also geared at:

- Supporting industry with its decarbonisation priorities, such as energy efficiency improvements and fuel switching;
- Developing new clean energy industries, such as green hydrogen production and export, and bioenergy;
- Workforce development, such as training existing workers in new technologies.

In response to concerns over the integrity of ACCUs and the crediting frameworks underpinning their generation, the new Federal Government has also commissioned a six-month review into the Australian carbon credit system.

An Independent Panel, led by Professor Ian Chubb, is currently reviewing the crediting and governance frameworks that have underpinned the historical ERF and ACCUs. This review will be informed by public consultation and meetings with academics, experts, First Nations groups, project proponents and developers, industry and consumer groups.

A final report with findings and recommendations is due by the end of 2022. This review process will ensure that Australia's carbon markets are fit for purpose and can support the task of industrial decarbonisation under a strengthened Safeguard Mechanism.

More Information

About the Emissions Reduction Fund <https://www.cleanenergyregulator.gov.au/ERF/About-the-Emissions-Reduction-Fund>

About The Safeguard Mechanism <https://www.dceew.gov.au/climate-change/emissions-reporting/national-greenhouse-energy-reporting-scheme/safeguard-mechanism>

Potential Futures for Australia's Safeguard Mechanism <https://carbonmarketinstitute.org/app/uploads/2022/06/Potential-futures-for-Australias-Safeguard-Mechanism.pdf>

Carbon Farming Industry Roadmap www.carbonmarketinstitute.org/roadmap