

22 September 2022

Safeguard Mechanism Taskforce
Department of Industry, Science and Resources
Submitted via email: safeguard.mechanism@industry.gov.au

Dear Sir/Madam

SAFEGUARD MECHANISM REFORM: CONSULTATION PAPER

On behalf of the Australian Council of Superannuation Investors (ACSI), thank you for the opportunity to make a submission related to the Safeguard Mechanism.

About ACSI

Established in 2001, ACSI exists to provide a strong voice on financially material environmental, social and governance (ESG) issues. Our members include 26 Australian and international asset owners and institutional investors with over \$1 trillion in funds under management.

Through research, engagement, advocacy and voting recommendations, ACSI supports members in exercising active ownership to strengthen investment outcomes. Active ownership, including the management of climate related risk, allows institutional investors to enhance the long-term value of retirement savings entrusted to them to manage.

This submission draws on the ACSI long-standing practice of detailed engagement with listed companies in relation to their management of climate-related risks and opportunities, as well as detailed research into market practices. ACSI supports the Paris Agreement goal of limiting warming to 1.5°C and net zero emissions by 2050. As part of this transition, policy makers will need to develop credible pathways to ensure an orderly and just transition to a net zero emissions economy. A planned transition will result in better economic outcomes, is better able to take account of the needs of various stakeholders and will enable better management of uncertainty and volatility.

ACSI is a member of the Investor Group on Climate Change. We support its separate submission to this consultation.

Summary of ACSI's position

ACSI welcomes the review of the Safeguard Mechanism. Limiting global warming to 1.5°C will require economy-wide emissions reductions. A well-designed Safeguard Mechanism using baseline levels that encourage industrial decarbonisation, consistent with limiting warming to 1.5°C, is one of several policy pathways required to meet Paris Agreement targets.

ACSI recommends that an updated Safeguard Mechanism design should support a least cost, orderly transition by:

- putting in place clear, credible and long-term baselines for covered facilities that encourage emissions reductions in line with Paris Agreement requirements,
- designing a credits system that ensures there are true incentives to invest in technological solutions for emissions reduction while recognising that individual sectors will have different transition pathways, and
- ensuring emissions reductions requirements are equitably spread across the market.

ACSI has some specific suggestions about how a revised Safeguard Mechanism could be strengthened. Our key recommendations are listed below.

Climate policy

A revision of the Safeguard Mechanism, with covered facilities contributing 28% of Australia's emissions¹, will be only one part of the required policy response to limit warming to 1.5°C. Individual sectors will have varying levels of difficulty in reducing emissions. Sectoral emissions reduction pathways will need to be identified and developed over time to reflect these diverse approaches to lowering emissions. Consequently, Government will need to implement policies that support the differing lower emissions pathways across different sectors and help guide investors considering their allocation of capital. Beyond the Safeguard Mechanism, Government should consider how to support innovation, an equitable and just transition, and reduced investment risk for early adopters of emissions reduction technologies. This could include long-term favourable financing options, direct support for project development through grants, tax incentives, and preferential treatment on import duties for components of low-carbon systems.

Baselines

ACSI welcomes the recalculation of baselines to enable the Safeguard Mechanism to support Australia's transition to a net zero economy. We support the establishment of an overall abatement requirement, on the basis that it would act to drive down emissions.² Baselines should align with technology and emissions pathways designed to limit warming to 1.5°C and with the sectoral emissions reduction pathways set by the Climate Change Authority. Baselines should be regularly independently reviewed and updated to support ongoing alignment with the goals of the Paris Agreement.

The performance of individual facilities against baselines should be subject to disclosure requirements, which are linked to the company's public reporting. There should also be consistency between company reporting and baseline requirements. For example, where companies have publicly expressed confidence in their strategy and business model's alignment with limiting warming to 1.5°C, this should support a company's ability to meet baseline requirements calculated on the same basis. Forty of the ASX200 companies have publicly released scenario testing using a 1.5°C model and many are already using a shadow carbon price.³

Safeguard Mechanism Credits (SMCs)

The design of the Safeguard Mechanism's credits regime has an important role to play in providing a credible investment signal and supporting an efficient transition at lowest cost. In order to encourage industrial decarbonisation, allowed credits for Safeguard Mechanism baselines should be restricted to SMCs, which are effectively capped by only being available when a facility has lower emissions than its baseline. The availability and price of SMCs should aim to provide the investment signals required to achieve actual carbon abatement by covered facilities. Allowing Australian Carbon Credit Units (ACCU) to also be used to meet baselines would inevitably lower the price of SMCs and dilute incentives to achieve lower emissions.

The proposed banking and borrowing of SMCs reflect that emissions reduction pathways may be lumpy rather than linear and that some sectors are harder to abate than others. However, the framework governing SMCs will need to be carefully structured to ensure facilities are incentivised to reduce their emissions as quickly as possible at lowest cost, and where required, invest in technology to do so. Any purchase of SMCs by facilities should be part of an overall, credible plan to reduce emissions and have appropriate disclosure requirements. Facilities banking or borrowing SMCs should be required to publicly report how the banking or borrowing of SMCs fits within their emissions reduction plan, the timeframe involved and update this disclosure on a regular basis to reflect technology or other market developments. The creation, transfer and surrender of SMCs should be publicly reported in a credible, timely and transparent manner.

¹ Department of Climate Change, Energy, the Environment and Water, *Safeguard Mechanism Reforms Consultation Paper*, August 2022, p.8.

² Department of Climate Change, Energy, the Environment and Water, *Safeguard Mechanism Reforms Consultation Paper*, August 2022, p.9.

³ <https://acsi.org.au/wp-content/uploads/2022/08/WEBSITE-VERSION-ACSI-Climate-Change-Disclosure-in-ASX200-designed-1.pdf>

Emissions Intensive Trade Exposed (EITE) facilities

The review contemplates that EITE facilities may receive additional assistance, whether through grants to invest in low emissions technology funding, the direct provision of Safeguard Mechanism Credits to these facilities, or through differentiated baseline decline rates.

ACSI recommends that the guiding focus of any additional assistance is the goal of emissions reduction. Low emissions technology funding would therefore be preferable to other proposed means of additional assistance. More generally, we are concerned that overall, assistance measures may act to increase the cost of transitioning to a lower emissions economy and distort market outcomes. As the world transitions to a low carbon economy, additional assistance may prolong business cases that are no longer viable. Over time, the growing presence of carbon trade adjusted policies, such as the EU's Carbon Border Adjustment Mechanism, can be expected to negatively impact the business model for emissions intensive Australian exports. Any additional assistance for EITE facilities should be in line with the following principles:

- a focus on assistance that enables carbon abatement in line with baseline requirements and promotes a timely, just and equitable transition to a low carbon economy,
- a clear and public rationale to justify the provision of additional assistance (e.g. technology development timelines) and a planned timeframe to meet the emissions reductions required by the baseline,
- a robust and rigorous process that ensure that emissions decline in line with the planned timeframe, and
- alignment with relevant sector de-carbonisation plans.

I trust our comments are of assistance. Please contact me or Brigid Richmond, ESG Analyst– Research and Policy (brichmond@acsi.org.au), should you require any further information.

Yours faithfully



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