

Environment & Planning Alert

Local government - managing cost increases for waste disposal under the Carbon Tax

May 2012

Outline

Local councils will pay more for waste disposal under the Carbon Pricing Mechanism (**CPM**) which is set to commence under the *Clean Energy Act 2011* on 1 July 2012.

The CPM, more commonly referred to as the Carbon Tax, contains particular complexities with respect to waste management services.

This Alert considers the principal issues that need to be considered by a local council which:

- operates a 'covered landfill' (being a landfill generating more than 25,000 tonnes of CO₂-e per annum), and is thereby directly liable for the Carbon Tax and needs to purchase carbon or other eligible units to account for emissions; or
- has entered into a waste services contract with a third party (eg. who undertakes waste collection services and operates an associated 'covered landfill'), and is thereby indirectly liable for the Carbon Tax via increased waste disposal prices, which seek to cover the additional impost imposed on the operator for their emissions.

In the first scenario, where a local council is directly liable for the Carbon Tax – the calculation of that liability is complex with respect to a 'covered landfill'. This Alert sets out the principal variables that need to be considered by a council which operates such facility.

In the second scenario, where a local council is indirectly liable for the Carbon Tax – any cost pass through claim

from a covered landfill operator will depend on the terms of the contract that the council has with its waste services provider. This Alert sets out the principal issues for a council to focus on when reviewing a current contract or negotiating a new one.

Key principles

It is important for councils to appreciate the following key principles:

- Waste deposited in a covered landfill generates 'pollution' (methane) over a long period of time - up to 40 years.
- The liability to pay for that 'pollution' arises when the pollution is actually generated - it is not an instant liability which arises when the waste is deposited in the landfill.
- A landfill operator can reduce (not eliminate) their carbon liability by destroying the 'pollution'. This occurs where there is a landfill gas (**LFG**) capture and destruction facility on the landfill.
- There is a complex scientific calculation required to determine the amount of taxable 'pollution' generated from a landfill in each year.
- A landfill operator would typically try to recover the total cost of the 'pollution' (methane) from the waste customer when the waste is deposited at the landfill. Hence, the landfill operator will try and collect funds to cover a liability **before** they have to pay the Carbon Tax.

- A landfill operator is therefore required to speculate about what price it has to pay over the 40 year period to account for the 'pollution'. Any price speculation is inherently uncertain as the future market price for carbon is only really known with certainty for the first three years of the scheme. The bulk of the landfill operator's liability arises **after** that three year fixed price period.
- Given the uncertainty about the amount of 'pollution' that has to be paid for each year (over such a long period), and the additional uncertainty about the cost of the pollution over that period, landfill operators and their customers need to work out how to share that risk.
- Contracts between landfill operators and their customers, and the contracts with their LFG destruction service providers need to be reviewed as a priority. Further, when new contracts are negotiated, care needs to be taken to address this issue so that both parties understand the risks that they are taking on.

Councils with direct liability

Councils who are directly liable under the CPM will be those who operate landfills that generate in excess of 25,000 tonnes of CO₂-e per annum. Mark Dreyfus QC, the Parliamentary Secretary for Climate Change and Energy Efficiency, has estimated that '*Councils that service population centres of 20,000 people or more*' are likely to exceed this threshold.

A local council reporting emissions from its landfill under the National Greenhouse Energy Reporting (NGER) framework will automatically be liable under the CPM.

As the operator of a covered landfill, the council may attempt to minimise its liability and ensure that it recovers costs from its customers which will enable it to meet the additional Carbon Tax liability.

The only effective way to reduce the size of this liability is for the council to ensure a LFG system is installed on the site. A LFG capture system burns the methane (ie. the 'pollution') thereby reducing the amount of pollution which attracts a liability.

A council with a LFG system should review its contract with its LFG service provider to determine the terms and conditions of the ongoing operation of that facility. To date, it has been usual for LFG systems to be operated without a fee being paid by the landfill operator (eg. the council). Councils should not assume this position will continue. It is likely that a fee will be required by the LFG operator to reduce the council's liability. Councils should

ensure that they properly understand the costs that may be required to be paid in future to ensure the ongoing operation of the LFG system.

As the carbon liability arises over a period of up to 40 years, the key question for a council is when does it collect the funds to pay this liability. There are two options:

- Firstly, the council could collect 100% of the funds at the time it receives the waste. This makes commercial sense for 'one-off' customers who deposit waste at a landfill and have no ongoing relationship with the council as the landfill operator.
- Alternatively, with regular customers, such as other local government authorities or large waste management service providers there is an opportunity for the council, as the landfill operator, to recover the costs of the carbon pollution in the future as the council will have an ongoing relationship with those customers who supply that waste.

Councils with indirect liability

Councils who are indirectly liable will be those who deliver waste to covered landfills that are operated either by private companies or other local government authorities. These councils are not directly liable for the pollution generated from the waste that is deposited at the landfill. However, as the landfill operators will incur costs associated with accepting the local council's waste, those landfill operators will try and pass that cost onto the council.

Councils need to budget for an increase in waste disposal costs of landfill disposal to reflect the anticipated increase in disposal costs. Again, there are two options:

- The first option is that the landfill operator might require an upfront payment for the entire liability associated with the waste that is delivered by the council to the landfill. This could be a significant payment.

It has been suggested by the landfill industry that a figure of \$30 per tonne might be required. In negotiating a position with the landfill operator, council should ensure it understands the total liability attached to the waste it delivers to the covered landfill.

For example, if the landfill does not have a LFG system, then there is no opportunity for the landfill operator to reduce its liability. By the same token, if there is a LFG system in place, the council should ensure it understands how effective that option is in reducing the pollution associated with council's waste

deposited at the landfill. Any reduction in the pollution from the LFG system reduces the costs incurred by the landfill operator and therefore should result in a lower cost being passed onto the council.

- The second option is for the council to pay the landfill operator for the carbon pollution associated with the waste in each year the waste generates pollution. In other words, the council might be best served by paying for the pollution as it is emitted rather than paying for the pollution when the waste is deposited. This would involve council agreeing to pay additional costs for waste disposal over many years.

From a budgeting point of view, a council needs to understand the likely risks associated with each option.

A council should therefore ensure that it carefully negotiates contracts with landfill operators to make sure that it fully understands the risks that it is taking, either in terms of making a payment when the waste is deposited, or ensuring that payments are made as the pollution is emitted. Given the size of the potential cost, this is an important commercial consideration.

Conclusion

A council needs to plan carefully to ensure that it can budget for the increase in costs associated with its waste collection and disposal services. The complexity surrounding the calculation of these liabilities should not be underestimated.

Local councils that operate landfills need to review their contracts with their customers to ensure that they can pass on the additional costs of operating a covered landfill.

Local councils which do not operate a landfill but have contracts to deliver waste to third party operated landfills are in a good position to negotiate sensible arrangements with their waste service providers to manage this cost increase into the future.

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