



Climate Change Alert August 2008

Greenhouse Gas Consumption & Destruction - what does the CPRS mean for these Opportunities?

The Implications of the Green Paper for the Waste and Forestry Sectors.

“ The effect of CPRS coverage is that only forestry will be eligible to receive permits (AEUs) whereas large landfill gas operations will receive no carbon support beyond the incentive to reduce their permit liability and small landfill gas operations will receive no “carbon support” whatsoever. ”

The Federal Government’s proposed emissions trading scheme is intended to take effect on 1 July 2010, and will be known as the Carbon Pollution Reduction Scheme (**CPRS**). A Green Paper on the design of the CPRS was released in July 2008.

This Alert focuses on the implications of the Green Paper for the waste and forestry sectors. Both sectors have the potential to reduce the amount of greenhouse gases (**GHGs**) entering the atmosphere.

Prior to the Green Paper being released, much was said about these two sectors providing opportunities for offsets, however the Federal Government is instead proposing that both waste and forestry be included as “covered sectors” from the outset of the CPRS in 2010.

Offsets v Scheme Coverage

There is a significant conceptual difference between eligibility to generate “offsets” and “scheme coverage”. Treating a particular industry as a covered sector can produce a very different outcome from giving that industry the opportunity to create offsets.

The reporting baseline for “covered sectors” is zero emissions. At the most basic level, if you emit GHGs you have

to acquire permits but if you sequester GHGs you receive permits. Forestry is the only “covered sector” likely to be a net carbon sink and hence entitled to receive permits - to be known as Australian Emissions Units (**AEUs**) – rather than being required to acquire them.

In contrast, the reporting baseline for “offsets” is business as usual emissions. The amount of offsets an activity can generate is equal to the resultant reduction in emissions over and above business as usual levels. However, the net emissions from that activity might still be greater than zero. For this reason, offsets can only come from emissions sources which are **not** covered by the CPRS.

Waste

The waste sector accounts for just over 3% of Australia’s GHG emissions.

The bulk of the waste industry’s contribution to GHG pollution comes from the degradation of waste stored in landfill which emits methane (a GHG with 21 times the Global Warming Potential of carbon dioxide).

The State based Environment Protection Authorities (**EPAs**) have recognised the need to control landfill gas as an environmental risk factor. Historically,



the concern has not been global warming but rather the risk of methane (an explosive gas) migrating from landfill sites to neighbouring properties. The bulk of the waste industry has therefore been managing its GHG emissions quite responsibly for some time without the need for a “carbon price signal” of the type contemplated by the proposed CPRS.

The NSW Greenhouse Gas Abatement Scheme has provided a carbon price signal for landfill gas operations in that State. In addition, the Mandatory Renewable Energy Target has promoted renewable energy sources such as landfill gas by requiring energy retailers and other large electricity users to purchase a specified proportion of their energy from accredited renewable energy sources. Significant investments have been made by the waste sector to manage greenhouse gas emissions from landfills in light of these carbon signals.

The Federal Government is proposing that the waste industry be a “covered sector”. This means that landfill gas facilities will be unable to generate offsets and landfill operators will instead have to account for the GHG emissions they generate. If the emissions threshold for participation in the CPRS is 25,000 tonnes of CO₂e per annum as for other covered sectors, approximately 100 large landfills will be covered but there will be no incentive (in terms of carbon) for smaller landfills to reduce their methane emissions.

This is a peculiar outcome given that the purpose of the CPRS is to reduce Australia’s total GHG emissions and landfill gas management systems are essentially a GHG **pollution destruction mechanism**. From a practical perspective, it also means that the CPRS will present new financial liabilities for the landfill industry rather than a new source of revenue.

Operators of landfill gas facilities should note that methane management systems may still need to be installed under State environmental protection and occupational health and safety laws.

Waste - Our View

Thomson Playford believes that upon closer analysis, there will be a number of unintended consequences of this type as a result of the Government’s preferred positions as set out in the Green Paper. “Smart technology” use by smaller businesses which has a positive greenhouse benefit may not be encouraged under the CPRS. This can only contribute to an increase in Australia’s greenhouse emissions and is not to be encouraged.

Forestry

Land-use, land-use change and forestry contribute approximately 7% to Australia’s greenhouse inventory. However, forestry has the potential to be a net sink of greenhouse gases and is one of the few cost-effective abatement opportunities currently available.

In recognition of this, the Federal Government is proposing that forestry be included in the CPRS on a voluntary basis from the outset of the scheme (rather than being eligible to create offsets):

- > forest managers who ‘opt-in’ will receive AEU’s representing the net increase of carbon stored in their forests.
- > forest managers will also be liable to surrender AEU’s for any net reduction in carbon stored in their forests (eg because of harvesting, bushfire or disease).
- > in accordance with Kyoto Protocol rules:

- only forests established after 1 January 1990 on cleared land will be eligible to create AEU’s.
- the forest must cover at least 0.2 hectares, the tree crown cover must be at least 20 per cent and the tree height must be at least two metres.
- natural forests, pre-1990 plantation forests and other forms of biosequestration (eg in soil and non-tree vegetation) will not be eligible to participate in the CPRS.

- > forest managers who don’t ‘opt in’ do not need to acquire permits in order to clear their forests. By the same token, they will not receive any permits for carbon sequestered during the life of the forest.

The benefits of CPRS participation will be greatest for owners of new forests (which have a greater sequestration potential than mature forests) planted for the purpose of permanently storing carbon. The benefits for harvest plantations will depend upon on the flexibility of harvesting schedules, future log prices and future carbon prices.

From a practical perspective, because forestry is likely to be a net sink rather than a net producer of GHG emissions, treating it as a covered sector under the CPRS will provide opportunities for new revenue streams in the same way as if forestry was eligible to create offsets.

Landholders who are considering planting forests for the purpose of participating in the CPRS also need to consider other regulatory issues such as water allocations and biodiversity implications.

Owners of harvest plantations who are deciding whether or not to participate in



the CPRS need to consider the implications of harvesting schedules, future log prices and future carbon prices when planning forest establishment and management.

Forestry – Our View

Overall, the proposed model for the forestry sector in the Green Paper is conservative, but internationally consistent. It presents minimal risks for forest managers and land owners, and some opportunities and incentives for those who have the land and resources to establish new forests to receive credits.

Conclusions

There are similarities between the waste-to-landfill and forestry sectors in that both activities have the potential to reduce the amount of carbon emissions from a given level of activity in the Australian economy. However, the effect of scheme coverage is that only forestry will be eligible to receive permits (AEUs) whereas large landfill gas operations will receive no carbon support beyond the incentive to reduce their permit liability, and small landfill gas operations will receive no “carbon support” whatsoever.

The next step

The Federal Government has called for submissions on the Green Paper by 10 September 2008. A White Paper setting out final government policy will be released in December 2008 along with an exposure draft of the proposed legislation.

If you would like to make a submission on either of these affected sectors, or on any other aspect of the Green Paper, please contact one of the people below.

For more information on this topic please contact:



Fraser Bell
Partner
+61 8 8236 1225
fbell@thomsonplayford.com.au



Shen Dycer
Lawyer
+61 8 8236 1227
sdycer@thomsonplayford.com.au



Alison Brookman
Special Counsel
+61 8 8236 1386
abrookman@thomsonplayford.com.au



John Howard
Partner
+61 2 8248 3401
jhoward@thomsonplayford.com.au

Adelaide

101 Pirie Street
Adelaide SA 5000
T: +61 8 8236 1300 . F: +61 8 8232 1961

Melbourne

Level 40, 140 William Street
Melbourne VIC 3000
T: +61 3 8608 7000 . F: +61 3 8608 7199

Sydney

Australia Square Tower
264 George Street Sydney NSW 2000
T: +61 2 8248 5800 . F: +61 2 8248 5899