

[original on EDL letterhead]

Building 17
2404 Logan Road
PO Box 4046
Eight Mile Plains Qld 4113
Australia
Main Tel 61 7 3275 5555
Main Fax 61 7 3341 5150

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Climate Change Group
Department of the Prime Minister and Cabinet
PO Box 6500
CANBERRA ACT 2600

By e-mail: emissionstrading@pmc.gov.au

Dear Sir/Madam

**Energy Developments Limited (EDL)
EDL Submission on the Abatement Incentives prior to the Commencement of the
Australian Emissions Trading Scheme Discussion Paper (Discussion Paper)**

EDL thanks the Climate Change Group for the opportunity to comment on the Discussion Paper and certain aspects of the proposed Australian Emissions Trading Scheme (**AETS**).

EDL's Background

By way of background, EDL is an international provider of independent, renewable and low greenhouse gas (**GHG**) emission energy. EDL operates in Australia, the United Kingdom, Europe and the United States, providing services in four main areas of power generation and associated energy solutions:

- Landfill gas (**LFG**) power;
- Coal mine methane (**CMM**) power;
- Remote area power; and
- Liquefied natural gas (**LNG**) and compressed natural gas (**CNG**) power.

EDL owns 64 power generation facilities internationally and, as at 30 June 2007, had a total installed generation capacity of 485 MW. EDL is one of Australia's largest carbon abaters, capturing and utilising approximately 8.5 million tonnes of GHG CO2 equivalent from its LFG and CMM power generation projects around the world in the financial year ended 30 June 2007.

EDL generates revenue from:

- Providing and selling low emission electricity to direct customers such as large energy retailers and mining companies;
- Generating and selling environmental credits in international, national and state based schemes; and
- Managing LFG related infrastructure on behalf of landfill owners.



As at 30 June 2007, EDL's Australian operations had a total installed capacity of approximately 327 MW. This total installed capacity is expected to increase to approximately 400MW with the progressive delivery of the predominantly LNG fuelled West Kimberley Power Project in Western Australia.

EDL's Australian customers are typically large 'blue chip' public companies and corporatised government bodies such as state-based energy retailers and landfill owners.

EDL abates significant quantities of Australian GHG

EDL is a significant player in the Australian GHG abatement scheme, and was an early mover in GHG abatement activities. EDL has seen GHG abatement activities flourish under the NSW Greenhouse Gas Abatement Scheme (**GGAS**), with the market for New South Wales Greenhouse Gas Abatement Certificates (**NGAC**) supporting this important activity, albeit that the NGAC market has recently been adversely affected by a number of factors, including, regrettably, previous AETS announcements.

While the Discussion Paper seeks comments on a relatively narrow set of issues, the topics covered by the Discussion Paper are broad, and EDL wishes to make comment on some of the more salient issues, as follows.

Firstly, it is acknowledged that key AETS details are yet to be devised, and that significant aspects of the AETS introductory and transitional arrangements are yet to be developed. However, EDL is concerned that the signals to date from the limited AETS details have tended to cloud the benefits provided by existing projects and existing abatement, particularly in relation to LFG and CMM power generation.

EDL would be concerned should the AETS fail to properly take account of existing projects and existing abatement and the GGAS support for these projects, in such a way as to effectively penalise market players with the foresight and vision to engage in pre-AETS GHG abatement or provide a perverse incentive to discontinue existing abatement activity, which in turn reduces displacement of high GHG electricity generation and consequently increases GHG emissions.

From a power generation perspective, EDL understands that AETS policy to date does not seek to favour any particular generation technology or fuel. However, EDL considers that there is a strong case to be made for supporting LFG and CMM power generation as part of the AETS framework for the following reasons:

- LFG and CMM power generation is carbon abatement – it displaces significant amounts of methane, a powerful GHG.
- LFG and CMM power generation displaces an equivalent amount of coal fired power generation.
- It makes sense to use and incentivise the use of LFG and CMM power generation rather than simply flaring the LFG and CMM – from a whole of system energy perspective, LFG and CMM are valuable energy sources and usage in power generation ought properly be maximised across the entire electricity supply equation, and appropriately encouraged by the AETS, just as it has been encouraged under GGAS.

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- LFG and CMM power generation is invariably embedded generation, reducing line losses and optimising the carbon footprint of the electrical energy available to the local network as compared with electricity generated far away with significant line losses.

EDL's Discussion Paper Submission

EDL's submission on the Discussion Paper is set out below, following the Discussion Paper headings and "issues for stakeholder consideration" format as applicable.

Summary of EDL's Discussion Paper Submission

In summary, EDL's main submissions and areas of concern in relation to the Discussion Paper subject matter are as follows:

- AETS interference with existing abatement schemes needs to be minimised, and to the extent that existing schemes are to be ended or merged into the AETS, this needs to be effected in a manner which encourages existing and new GHG abatement activity alike, and which does not provide a perverse incentive to discontinue existing electricity generation abatement activity and consequently increase GHG emissions. EDL proposes this be best achieved by grandfathering existing electricity generation abatement projects so that they can produce AETS offset credits for the life of the grandfathered project, even if the project is otherwise in a covered sector.
- To the extent that existing GHG abatement activities do suffer disproportionate loss and are not otherwise benefited from the AETS (eg through grandfathering and being permitted to create offset credits), then compensation should be full and assess lost or foregone revenue from green credit/abatement certificate sales based on either applicable contract green credit/abatement certificate prices, or (if absent), the relevant market price disregarding any negative impact attributable to the AETS (eg disregarding market price reductions following AETS announcements). Also, disproportionate loss compensation should be absolute – ie not subject to any contractual clawback or adjustment.
- The criteria for assessing a project or asset "in existence" should be a flexible assessment of whether the project or asset was commercially committed to, with no realistic commercial opportunity to withdraw and "re-write" the underlying financial commercial and financial aspects of the project, and the project should also commence functional and commercial operation prior to the AETS.
- A new project or asset which is "in existence" should be entitled to both compensation and early action credits, albeit that the early action credits may reduce the compensation. These are not inconsistent concepts: compensation is for the life of project or asset, whereas early action credits apply from project commercial operation up to AETS commencement.
- Emissions permits derived from early action credits and the compensation process should be fully bankable.

Discussion Paper Chapter 2 – Ensuring allocation rules maintain abatement incentives

Discussion Paper Item 2.1 – ‘No disadvantage’ arrangements

Discussion Paper Issue: “It is proposed that the emissions trading scheme regulator use verified emissions data from the first mandatory reporting period under the National Greenhouse and Energy Reporting System as an input into permit allocations. It is proposed that the regulator supplement this with verified abatement data from the previous year and draw on other relevant sources of data where this would assist in ensuring firms receive an appropriate allocation of permits.”

EDL considers that defining an appropriate baseline period from which to assess emissions profiles and in turn determine appropriate permit allocations is critical to the fair and efficient operation of the AETS, and to ensure that the AETS applies in an environmentally efficient manner.

Accordingly, EDL supports the Discussion Paper proposal in this regard as representing one significant input in this process, but EDL considers that other relevant considerations and factors need to be taken into account in assessing the baseline, to the extent they are available or relevant, namely:

- using robust and supportable data from other relevant periods prior to the first mandatory reporting period and the previous year (**Prior Relevant Data**) – EDL does not support limiting the data review to just the first mandatory reporting period and the previous year; and
- adjusting for the impact of material “one off” deviations from “business as usual” emissions which would otherwise distort the emissions profile under assessment (**One Off Adjustments**).

(Of course, if there was no Prior Relevant Data or no One Off Adjustments, then the permit allocation assessment could be made having regard to only the verified emissions data from the first mandatory reporting period and the previous year.)

EDL notes the following in support of the proposition for including One Off Adjustments and Prior Relevant Data:

- EDL’s power generation activities and therefore emissions profile is subject to occasional material deviations and One Off Adjustments. For example:
 - CMM generation varies as a consequence of changes in coal mining activities – eg a mine operator decision to move a longwall invariably produces a swing in CMM generation from an initial reduction to a subsequent increase.
 - EDL uses modular power generators which can be moved from site to site and an emissions profile should take account of site specific relocations.

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- From a statistical perspective, having a broader timeframe than just the first mandatory reporting period and the previous year should, generally speaking, give a more accurate assessment of an emissions profile, taking into account deviations from “business as usual” emissions which may not be considered to be sufficiently “material” to justify a One Off Adjustment.

As stated above, EDL considers that Prior Relevant Data ought be robust and supportable: in this regard, EDL considers that the accuracy of some emissions data can be tainted where reporting of emissions has historically been carried out by one entity, yet reporting of abatement has been carried out by a second entity and where emissions occur as a consequence of the activities of both parties. Such a situation may arise at LFG and CMM generation sites, where EDL generates power from fugitive emissions arising from the activities of the landfill and coal mine sites respectively. Clarity is sought in better understanding the manner in which such instances will be managed.

EDL’s Comment:

EDL supports the use of data from the first mandatory reporting period under the National Greenhouse and Energy Reporting System and the previous year as one relevant input into permit allocations, but not as the sole relevant input in this process. To mitigate against biased information, EDL further proposes:

- the use of averaged emissions data over a previous number of years using methodologies similar to those the Renewable Energy (Electricity) Regulations 2001 (where such data is available) – EDL suggests a 4 to 5 year period as being optimal in this regard, and EDL supports the use of older versions of the Australian Greenhouse Office’s Factors and Methods Workbook to streamline emission factors nationally for these historical periods; and
- the ability to adjust for the impact of material “one off” deviations from “business as usual” emissions which would otherwise distort the emissions profile under assessment.

EDL also seeks clarity about how historical data will be used in instances where reporting of historical emissions is carried out by one party, reporting of abatement is carried out by a second party and where the emissions arise due to the activities of both parties.

Discussion Paper Issue: “Firms are encouraged to report abatement through the National Greenhouse and Energy Reporting System along with other corporate emissions and energy data, and to keep high quality records of abatement activity in the mean time. Stakeholder advice is sought on relevant sources of data outside of NGERs that could be used for this purpose (eg, information from environmental approval processes or greenhouse or energy use programmes such as Energy Efficiency Opportunities).”

EDL supports reporting of abatement through the NGER System, in addition to other corporate emissions and energy data. As discussed above however, EDL is concerned that this can be problematic where abatement and emissions are reported through alternative reporting regimes with different reporting criteria and boundaries (eg the contrast between the Energy Efficiency Opportunities and NGER System boundaries).

EDL's Comment:

EDL supports reporting of abatement through the NGER System, in addition to other corporate emissions and energy data.

Guidance is sought in the management of abatement data where the data is derived from alternative emissions and energy reporting regimes with conflicting boundary definitions.

Discussion Paper Item 2.2 – Assets eligible for compensation

Discussion Paper Issue: “Stakeholder feedback is being sought in relation to the definition of an asset “in existence” at the cut-off date. Feedback is sought in relation to the guidance afforded by the use of the National Electricity Market (NEM) definition and criteria for the electricity generation sector, and any necessary amendments to the criteria that may be necessary to give a similar outcome for other industries.”

As an initial comment, EDL seeks clarification on whether it is in any way intended that a project or an asset taken to be “in existence” cannot create early action credits. It is EDL’s understanding of the Discussion Paper that this is not the intention, and that a project or an asset taken to be “in existence” could, subject to satisfying other relevant criteria, be entitled to both:

- receive disproportionate loss compensation; and
- generate early action credits.

EDL seeks clarification on this issue, and EDL’s following comments are based on the understanding that the underlying AETS policy on this issue is as set out above.

EDL is concerned that the NEM “committed project” is overly restrictive in determining whether a project or an asset is “in existence” and accordingly eligible for disproportionate loss compensation. EDL notes that the NEM assessment criteria is that:

“Once a project satisfies all five criteria, it is considered by NEMMCO to be ‘committed’. A committed project is considered to have a high probability of proceeding to completion”.

EDL does not consider the NEM “committed project” definition to be a fair test of a committed project or asset “in existence” and therefore whether it is eligible for disproportionate loss compensation.

EDL submits that disproportionate loss compensation should apply for projects and assets which:

- are commercially committed to and where there is no realistic commercial opportunity to withdraw and “re-write” the underlying financial commercial and financial aspects of the project to attempt to take into account the unknown impact of AETS implementation; and
- commence functional and commercial operation prior to the AETS.

The assessment of “commercially committed” and “no realistic commercial opportunity to withdraw” needs to take into account the significant risk that would be involved in a transactional party seeking to be extricated from the project, including reputational risk, legal risk (eg risk of being sued), and financial risk (eg having to write off project development and planning expenditure).

EDL also notes that many circumstances may arise where projects are commercially committed to without the NEMMCO five criteria having been attained. For example, where project partners have previously engaged in identical project types, project partners may be commercially committed to a new project where some but not all of the NEMMCO five criteria are attained – eg formal arrangements or agreements such as land tenure/leases or exact financing arrangements may not be formally concluded, with the parties having commercially committed to the project on the basis that these matters are a manageable formality.

EDL considers that a “tick the box” approach akin to the NEMMCO five criteria is inappropriate for the relevant purposes, and that the assessment needs to be more flexible, with a project or an asset being taken to be “in existence” if it is commercially committed to and where there is no realistic commercial opportunity for a transaction party to withdraw.

EDL Comment:

EDL does not consider the NEM “committed project” definition to be a fair test of a “committed project” and therefore whether it is eligible for disproportionate loss compensation. EDL submits that a fair test is whether, as at 3 June 2007, the project was commercially committed with no realistic commercial opportunity to withdraw, and subsequently commences functional and commercial operation prior to the AETS.

As a separate issue, EDL considers that:

- disproportionate loss compensation should be absolute – ie not subject to any contractual clawback or adjustment provided the relevant contractual clawback or adjustment was agreed at or prior to 3 June 2007; and
- compensation be full and should include an assessment of lost or foregone revenue from green credit/abatement certificate sales based on either applicable contract green credit/abatement certificate prices, or (if absent), the relevant market price disregarding any negative impact attributable to the AETS (eg disregarding market price reductions following AETS announcements).

Chapter 3: Positive incentives to undertake additional abatement

Discussion Paper Item 3.1 – Standards for abatement recognised by the scheme

Discussion Paper Issue: “It is proposed that credits only be provided for activities that represent abatement that has actually occurred, is additional, permanent, measurable, and verifiable.”

EDL is generally supportive of this proposal, with a qualification regarding the requirement that abatement be “additional”. EDL seeks clarification on the detailed criteria proposed to assess additionality, particularly in the context of LFG and CMM, where there may be “obligations” imposed on the landfill owner or coal mine owner (as the case may be), or EDL, or both, to flare LFG or CMM (as the case may be). EDL submits that the use of LFG and CMM to generate electricity ought to be considered to represent additional abatement of the LFG/CMM irrespective of any other legal reference to LFG/CMM flaring.

In this regard, EDL currently operates across multiple Australian sites, each with differing legislation applicable to LFG and CMM. Using LFG as an example, a requirement to flare (in the absence of alternate power generation use) can be imposed from the perspective of mitigating LFG associated odour, rather than based on GHG reduction criteria. As a consequence, EDL is concerned that there may be the potential for activities to be deemed to be “additional” in one location, with the same activity being deemed to be “not additional” in another, in the absence of a clear provision appropriately treating LFG/CMM power generation usage as being additional, as the use in power generation *per se* reduces overall GHG emissions.

EDL Comment:

EDL seeks clarification on the additionality criteria applicable to LFG and CMM, and submits that LFG and CMM power generation usage ought properly be treated as being additional without exception.

Discussion Paper Item 3.2 – Eligible activities

Discussion Paper Issue: “It is proposed that there be no restriction on the types of activities that can earn credits prior to 2011 for use in the emissions trading scheme, provided they represent abatement that is additional, has actually occurred, and is permanent, measurable, and verifiable.”

Subject to EDL’s prior comments, EDL supports the proposition that there be no restriction on the types of activities that can earn early action credits for use in the AETS. EDL notes that appropriate transitional arrangements will need to apply to take account of the current credits generated under GGAS, and AETS early action credits.

EDL Comment:

EDL supports the lack of restrictions imposed on the types of activities that can earn AETS early action credits.

EDL's position in this regard is on the basis that:

- a project or an asset taken to be "in existence" could, subject to satisfying other relevant criteria, be eligible for disproportionate loss compensation and be eligible to generate early action credits;
- the criteria for assessing projects and assets "in existence" be widened; and
- LFG and CMM power generation usage be treated as being additional.

Discussion Paper Issue: "It is proposed that early action credits be generated from eligible projects for abatement after 3 June 2007 until the commencement of the scheme due in 2011. Similarly, it is proposed that offset credits for use in the emissions trading scheme can be generated from eligible projects for abatement after 3 June 2007. To be eligible, it is proposed that projects would need to be established after 3 June 2007."

EDL supports the generation of early action credits and offset credits for use in the AETS from eligible projects for abatement from 3 June 2007 to the start of the AETS.

However, EDL considers that electricity generation projects that have been previously accredited or selected under other State/Federal government programmes as offset projects or as eligible for government funding (eg GGAS) should be grandfathered into the AETS and entitled to:

- generate AETS early action credits;
- convert outstanding certificates (eg NGACs) into AETS early action credits or offset credits; and
- produce AETS offset credits for the life of the grandfathered project (even if the project is otherwise in a covered sector),

if such other State/Federal schemes cease to exist upon or prior to AETS commencement, or otherwise due to the AETS.

EDL has committed (prior to 3 June 2007) to numerous projects that generate electricity from fugitive emissions arising from both CMM and LFG. These projects have flourished with the support from the other State/Federal government programmes, especially the NGACs attributable to the GGAS, and from an additionality perspective, have a significant GHG abatement impact.

EDL submits that the AETS should not unfairly impact upon parties such as EDL which have engaged in early abatement activity, nor should the AETS act as a perverse incentive to shut down existing abatement activity, thus increasing GHG emissions.

Hypothetically speaking, were a CMM/LFG generator not to continue electricity generation due to AETS related disincentives, then significant environmental losses would be expected to occur, each going against the principal driver behind the introduction of the AETS:

- 1) renewable energy would no longer be generated;
- 2) the displacement of an equivalent amount of coal fired power generation would cease; and
- 3) GHG emissions would likely increase.

EDL considers that appropriate transitional or grandfathering mechanisms are required to facilitate the continuation of existing electricity generation abatement activities, and that this aspect of the AETS needs clarification.

Using GGAS as a particular example, EDL considers that, should GGAS be discontinued or superseded by the AETS, then EDL should be able to:

- generate AETS early action credits from the end of GGAS to the start of AETS, assessing abatement on the same basis as for GGAS (ie 1 tonne of CO₂-e accredited under the GGAS scheme should be counted as 1 tonne of CO₂-e accredited under the AETS as an early action credit);
- convert any outstanding un-surrendered NGACs into AETS early action credits or offset credits, again assessing abatement on the same basis as for GGAS; and
- produce AETS offset credits for the life of the grandfathered electricity generation project, again assessing abatement on the same basis as for GGAS.

EDL Comment:

Clarification is sought on the treatment of abatement electricity generation projects previously accredited, or selected, under State/Federal government programmes as offset projects or as eligible for government funding, where such schemes cease to exist upon or prior to AETS commencement, or otherwise due to the AETS.

EDL proposes that such electricity generation abatement projects should be grandfathered into the AETS and entitled to transfer the value of the proposed credits / abatement achieved at an equivalent rate of 1 tonne of CO₂-e, and to produce AETS offset credits for the life of the grandfathered electricity generation project (even if the project is otherwise in a covered sector).

Discussion Paper Issue: “Abatement projects could only be approved following final decisions as to eligibility of activities for offsets or early action credits for use in a future emissions trading scheme.”

EDL Comment:

EDL supports this statement, subject to the earlier comments regarding existing abatement projects.

Discussion Paper Item 3.3.1 – Initial arrangements – approval via Greenhouse Friendly

Discussion Paper Issue: “It is proposed that the Australian Government’s Greenhouse Friendly programme provide the initial administrative mechanism for approving offsets and early action credits for use in the emissions trading scheme.”

EDL generally supports the proposition that the Australian Government’s Greenhouse Friendly programme provide the initial administrative mechanism for approving offsets and early action credits for use in the AETS.

However, EDL understands that some aspects of the current Greenhouse Friendly programme lack transparency in comparison with other offset regimes (eg Clean Development Mechanism Project Design Documents, Approved Methodologies, verification reports etc). EDL would expect the Greenhouse Friendly programme would achieve similar levels of transparency should it become part of a legislated emissions trading regime.

EDL Comment:

EDL supports the proposition that the Australian Government’s Greenhouse Friendly programme provide the initial administrative mechanism for approving offsets and early action credits for use in the AETS.

EDL propose however that the underlying Greenhouse Friendly programme documentation and processes become more accessible and transparent.

Discussion Paper Issue: “It is proposed that the existing Greenhouse Friendly protocol for new forest offsets be used to assess eligibility following any Government decision, but be reviewed in 2008.”

EDL Comment:

EDL supports this proposition, subject to the earlier comments regarding improved Greenhouse Friendly programme transparency, with the review process to be subject to stakeholder consultation.

Discussion Paper Item 3.3.2 – Streamlining administration of offsets and early action credits

Discussion Paper Issue: “It is proposed that streamlined protocols be developed for eligible early action and offset projects. Stakeholder feedback is sought on priority project activities for protocol development.”

EDL Comment:

EDL supports this proposition, and suggests the use of existing NGAC protocols and approved CDM methodologies for consistency and familiarity with current Australian practice

and to facilitate timely development of the required protocols.

Discussion Paper Item 3.4 – National register for offsets and early action credit

Discussion Paper Issue: “The Government proposes to develop as soon as practical a national offset register to track early action credits and offsets that could be recognised under the emissions trading scheme.”

EDL supports this proposition.

Discussion Paper Item 3.6 – Transitioning early action credits into the emissions trading scheme

Discussion Paper Issue: “It is proposed that the scheme regulator exchange early action credits for emissions permits dated for use in the first year of the scheme.”

EDL understands that it is intended that, while early action credits are to be exchangeable for emissions permits dated for use in the first year of the scheme, these emissions permits are fully bankable and so could be used or sold in any subsequent AETS year. On this basis, EDL supports the proposition, and EDL notes that the ability to bank permits from the earlier years of an emissions trading scheme (where the price may be lower), can assist greatly to protect against volatile prices in future years of the scheme.

EDL would be grateful for clarification on this point, and if it were intended that early action credits/AETS year 1 emissions permits not be fully bankable, then EDL would not support such a proposal.

EDL Comment:

EDL supports the proposition that early action credits be exchanged for emissions permits dated for use in the first year of the scheme and bankable for use or sale in any subsequent AETS year.

Discussion Paper Issue: “It is proposed that there be no limits on the number of early action credits that would be recognised.”

EDL Comment:

EDL supports this proposition.

Discussion Paper Issue: “It is proposed that early abatement be taken into consideration when setting the emissions caps in the initial phase of the scheme.”

EDL Comment:

EDL supports this proposition, subject to the comments above about setting an appropriate baseline period from which to assess emissions profiles and on the basis that early abatement should include any abatement undertaken as a consequence of other schemes (eg GGAS), with 1 NGAC to be equivalent to 1 tonne CO₂-e.

Discussion Paper Item 3.8 – Voluntary market access to offsets accredited for use in the emissions trading scheme

Discussion Paper Issue: “It is proposed that participants in the voluntary market would have access to early action credits and offsets credited for use in the emissions trading scheme.”

EDL supports the access of participants in the voluntary market to early action credits and offsets credited for use in the AETS. In promoting a healthy carbon price in both the mandatory and voluntary markets, it is important that competition for early action credits and for offsets remains strong. Were access to early action credits and offsets be denied to the voluntary market, then competition within the mandatory market might remain weak, potentially discouraging abatement activities. By encouraging voluntary market participants, and thereby increasing liquidity in the market, EDL considers that such competition is promoted.

EDL Comment:

EDL supports this proposition.

Again, EDL thanks the Climate Change Group for the opportunity to comment on the Discussion Paper.

Please do not hesitate to contact us should you wish to discuss any aspects of our comments.

Yours faithfully

[original letter signed]

Greg Pritchard
Finance Director
Energy Developments Limited