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Greenhouse Gas Reduction Scheme Transition Review
Department of Water and Energy
GPO Box 3889
SYDNEY NSW 2001

16 April 2008

Dear Sir/Madam

**Transitional arrangements for the NSW Greenhouse Gas Abatement Scheme
(GGAS): Consultation paper**

I have been closely involved in the design and operation of GGAS since its inception as a voluntary program in 1997.

I was the author of the original Methodology Workbook (July 1997) and all subsequent revisions. In 2002 I worked intensively on the transition from a voluntary scheme to the present regulated scheme. I prepared the original methodologies for Rule 1 (Compliance), Rule 2 (Generation), Rule 4 (Large User Abatement Certificates) and Rule 5 (Carbon sequestration). While I did not actually draft Rule 3 (Demand Side Abatement) I had considerable input into the development of that methodology as well.

I am also currently involved in the development of the proposed National Emissions Trading System (NETS).

Based on my familiarity with the origins and structure of GGAS, my views are that:

1. There is no policy rationale for formally linking any aspect of GGAS (a limited baseline and credit scheme) to NETS (a national cap and trade scheme). In particular,
 - (a) there is no case for requiring any 'compensation' for GGAS participants from NETS, eg via free allocation of emissions permits or any other mechanism;
 - (b) there is no case for binding or constraining any aspect of NETS design to accommodate any aspect of GGAS, whether in the treatment of 'offsets' from the combustion of waste methane or any other element.
2. The case for *any* 'compensation' to GGAS participants is very weak. The NSW Government always made it clear that the rationale for GGAS was the absence of a national cap and trade scheme and that GGAS would become

redundant when such a scheme was established. Participants were therefore always in a position to make their own judgements about the likelihood and timing of a NETS, whether their actions or projects would continue to have value under NETS (most will) and if not, whether they would make adequate returns prior to NETS;

3. If however the NSW Government feels that 'it is important to protect the legitimate business interests of those who have responded to the investment incentives created by GGAS' (p7 of CP) and that there is a case for compensation, it should be provided entirely within the framework of GGAS – either by transfers from those who stand to benefit from early abandonment (eg liable parties) or by payment from the NSW and ACT Governments.
4. If any GGAS participants wish to make a case for compensation to the NSW Government, they should be required to:
 - (a) prove that the claimed loss results from actions or investments that were undertaken after the commencement of GGAS in 2003 (this excludes all Category A Generators, for example);
 - (b) prove that the actions or investments would not have been undertaken but for the existence of GGAS (ie after allowing for other influences, including normal capital replacement cycles, MRET, the Greenhouse Challenge program, the Generator Efficiency Standards program, the Queensland 13% gas program etc etc);
 - (c) quantify the expected reduction in benefit between the now likely date of termination of GGAS and the date previously discussed (end of 2012);
 - (d) take into account the expected benefits from the NETS over that period.
5. Any compensation should take into account the likelihood of continuing downward pressure on NGAC prices from the excess of certificate creation over demand between 2003 and 2007 (p 57, *Compliance and Operation of the NSW GGAS during 2006*, IPART, July 2007).

Comments in relation to numbered sections in the Consultation Paper

4.1 Transitional Timeframe

A time period is only relevant if there is a question of some form of compensation for losses incurred, or losses incurred later as a result of actions taken, during that period.. I argue that there is no case for compensation, so the timeframe is not relevant.

4.2.1 Fossil Fuel Generators

I support neither option. The possibility of one-off compensation for 'disproportionate loss of value' was raised by the previous Federal Government, but has not been endorsed by the present Government. Whether a party has participated or continues to participate in GGAS (or any other State or Commonwealth program terminated once NETS commences) should have no bearing on how NETS permits are allocated or on how any funds raised from auctioning of NETS permits should be disbursed.

4.2.2. Waste Coal Mine Methane (WCMG) generators and landfill gas

The capture of WCMG will continue to have value under NETS because it will avoid the need to acquire permits for the emission of methane (although permits for emission of the CO₂ from the combustion of the captured CH₄ would be required). Landfill gas generation will continue to have value because only the non-CO₂ emission from 'renewable' fuels will need permits. Therefore no special provisions are necessary. .

4.2.3 Category A Generation

GGAS has resulted in a windfall for the owners of Category A generation, while the marginal effect on greenhouse gas emissions (beyond what would have occurred in the absence of GGAS) is close to zero. Therefore no special provisions are necessary.

4.2.4 Carbon Sequestration Projects

Whether or not forest carbon sequestration projects accredited under GGAS (or any other such projects, for that matter) might eventually receive accreditation to create carbon offsets under NETS is a matter for NETS.

The GGAS rules place an obligation on such projects to 'maintain the Greenhouse Gas abatement secured by Carbon Sequestration Activities for 100 years from the Compliance Year in which NGACs may be registered (Rule 5, Clause 5c). It was always made clear that this obligation would survive the termination of GGAS.

The Rule also notes that 'The Kyoto Protocol, if it comes into force, will not give credit for any sequestration of carbon in Forests on Kyoto-Consistent Land that takes place prior to 2008 and thus has no direct bearing on the operation of this Rule up to that date. However, there may be some indirect interactions in that obligations arising from the creation of NGACs prior to the first Commitment Period will have to be maintained.'

Forest carbon sequestration project operators have all the notice they need to decide whether to reserve carbon stock increments from July 2007 (the probable beginning of Australia's first Kyoto Commitment Period) for possible sale into the NETS or whether to continue to create NGACs. Therefore no special provisions are necessary.

4.2.5 Large User Abatement Certificates

As the need for large users to surrender NGACs/LUACs will terminate at exactly the same time as the value of the LUACs, no special provision is necessary.

4.2.6 DSA abatement certificates

For DSA Certificates created under the Default Abatement Method, the full lifetime impact of measures has already been brought to account and the creators of such certificates have already realised the full value through the creation of NGACs. I estimate that about 80% of the DSA NGACs created so far are in this category. Therefore no special provisions are necessary.

For other DSA activity, the NSW Government (alone or with other Governments) is free to set up a 'White certificate' program in parallel to the NETS if it wishes, and to credit any new NGAC value that would have been created to 2012 against that new program.

4.3 Unused abatement certificates

The Consultation Paper (p12) states that:

'However, it will be important that transitional arrangements for unused NGACs do not create incentives to:

- create more NGACs than would otherwise have been supplied up to the start of the NETS, in order to take advantage of transition options;
- hold NGACs and restrict their supply to liable parties in the lead-up to the NETS; or
- for liable parties under GGAS to hold NGACs and fail to comply with GGAS, choosing instead to pay the GGAS penalty.'

The most effective way to avoid these outcomes is to announce immediately that NGACs will not be exchangeable for emission permits, that the value of unused NGACs will be extinguished at the end of 2012 and that there are no 'transition options' to 'take advantage of'. If this is unacceptable, then it is the responsibility of the NSW Government alone (not the Commonwealth or the NETS) to compensate for any (demonstrable) loss of value.

4.4 New Accreditations

If new accreditations are to be accepted it should only be on condition that applicants forego any claim for possible compensation in the event that the NSW Government should decide to make such arrangements.

I trust these comments are helpful,

Yours faithfully

George Wilkenfeld