29 September 2017

Climate Change Authority
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Dear Climate Change Authority,

Submission on Consultation Paper: Review of the Carbon Farming Initiative (CFI) Legislation and the Emissions Reduction Fund (ERF)

Thank you for your invitation to provide a submission on the Consultation Paper released in August 2017 in relation to the review of the Carbon Farming Initiative Legislation and the Emissions Reduction Fund.

Founded in 2003, Climate Friendly Pty Ltd is one of Australia's largest, most experienced carbon farming project developers. Climate Friendly's Carbon Farming Team has more than 20 expert staff, with significant experience in agriculture, forestry, broad scale land management, training, Aboriginal consultation, and working with all levels of government. We have a proven track record:

- established partnerships with around 100 landholders across Australia;
- 100% success rate with our project audits;
- delivering over 40 million tonnes of contracted carbon abatement with the Australian Government; and
- Emissions Reduction Fund contracts with a total value in excess of $500 million for our landholders under our portfolio management.

We welcome the CFI and ERF Review given the importance of this policy and legislative platform as a mechanism to address climate change and reduce emissions. We understand that this review is focused on the operational aspects of the ERF, and provide some targeted responses to consultation questions at **Attachment 1**. We have also provided some general comments in this covering letter.

Achievements of the ERF:

In general we would like to **highlight the achievements** of the CFI and ERF to date, particularly in terms of land sector projects.

- More than **25 million ACCUs have already been issued for land sector projects** (under agriculture, savanna and vegetation methods);
- There has been significant uptake of regeneration and savanna methods, with more than 180 human-induced **regeneration projects spanning nearly 7 million hectares**, primarily in south-west Queensland and north-west New South Wales, and over 70 **savanna projects covering more than 30 million hectares** in northern Australia.
- ACCUs already issued for land use projects in regional Australia are worth more than **$300 million for landholders in regional Australia** (based on average auction price). Contracted ACCUs for land use projects are worth more than $2 billion on the same basis.

This amounts to **transformative change in the regions where these projects occur**, both from a sustainable land management and an economic perspective. This is a significant achievement since the commencement of the CFI and the ERF, and it is imperative that this good news story is shared across the industry and with the broader Australian public.

Challenges and opportunities for improvements:

While the scheme has delivered substantial achievements as outlined above, there is also significant room for improvement and increased operational efficiencies. Although long-term government contracts have offered a price signal with lower risk, **development of deep, liquid carbon markets remains imperative** to deliver the level of abatement required.

Additionally, many of the ERF systems and processes remain under development and would benefit from simplification. Further, while some land sector methods have had high uptake, the array of **methods and eligibility criteria are, in part, impacting the ability of some regions to participate in the scheme.**

Further, under the current methodological rules, we are failing to fully account for the abatement actually delivered, due to methods that focus on a single abatement activity while additional abatement, outside the scope of the method, is commonly also delivered as part of the project activities. Moreover, opportunities beyond the land sector are largely unviable at the current average carbon price. Extended timeframes or stagnation in method development, combined with inability for project developers to prepare their own methodologies, and uncertainty around funding or market sources beyond the ERF, are already limiting the level of ongoing project development, with operational implications for the ERF.

Policy certainty & ambitious national targets:

Climate Friendly was founded as a profit-for-purpose company. We have ambitious targets to deliver environmental outcomes, acting with urgency, innovation and stewardship.

In line with our goals as a company and our desire to support Australia to achieve, and indeed exceed, our national targets, we note the Climate Change Authority's findings in the *2016 Special Review on Australia's Climate Goals and Policies*. In particular, we note the findings around:

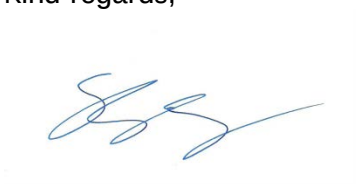
- the substantial opportunities for emissions reductions in agriculture and land use across Australia;
- the capacity of a market mechanism to allow Australia to meet its emissions reduction targets at lower cost; and
- the impact of uncertainty and frequent changes in direction observed in the report, coupled with the ability to strengthen and build on existing policy and regulatory platforms to provide a toolkit for delivering on Australia's Paris Agreement obligations.

In considering operational aspects of the ERF, it is important to keep these broader policy and regulatory issues at the forefront - **without the right pricing signals and policy toolkit, improvements to the operational aspects of the ERF will not deliver Australia's contribution towards the Paris Agreement and tackle the pressing issue of climate change**.

Please do not hesitate to contact me if I can provide any additional information regarding responses provided as part of this submission.

Climate Friendly looks forward to the Climate Change Authority's report, and to continuing to participate in the ERF as a key mechanism delivering Australia's contribution towards the Paris Agreement.

Kind regards,



Skye Glenday
Head of Strategy & Risk

Attachment 1: Response to Consultation Questions

1. ERF Methods: questions 1, 2, 4, 5, 6

As outlined in the general comments above, the vast majority of projects registered and ACCUs issued fall under a limited number of project methods, namely avoided deforestation, human-induced regeneration and savanna burning in the land sector, and landfill gas outside the land sector. In our opinion, this does not constitute sufficient coverage of emissions reduction opportunities at a project level across Australia. In addition to projects being largely registered under a few methods, they are also primarily located in two regions of Australia, across northern Australia and clustered around south-west Queensland and north-west New South Wales. This distribution is a by-product of the opportunities covered by methods that have more readily had uptake. This means there are substantial opportunities in the remainder of the country that have not yet been optimised.

While there are a number of other methods with limited uptake, 7 methods have no registered projects and only 12 methods have projects that have to date been issued ACCUs. This is in part owing to the fact that many developed methods have limitations in eligibility criteria, or implementation challenges that render them commercially or logistically unviable. An example of methods that face these challenges includes the soil methodologies, with no projects currently registered under the default measurement methodology and 30 projects registered, but no ACCUs issued, for projects under the measurement methodology. The eligibility criteria for many methods are overly specific, meaning a minor deviation from the criteria renders a project ineligible, even though the proposed activities would deliver genuine abatement in line with both domestic and international offset integrity standards.

Consequently, Climate Friendly suggests that some method eligibility criteria could be made less prescriptive (i.e. could be converted to principles, rather than criteria). This would open up the potential for case-by-case assessments of project eligibility, which would be subject to audit. Whilst this places a greater onus on auditors to assess technical merits of a project, it increases the flexibility of eligibility criteria, thereby potentially increasing the pool of projects that can apply and the quantum of abatement that can be delivered. There are precedents for this type of assessment, for example certification under the Forest Stewardship Council, which relies on an auditor's assessment of 10 Principles.[1]

Additionally, several land-sector abatement activities exist that are currently not accounted for in Australia's national accounting (pasture carbon pools, sub-optimal carbon levels within "forest cover" vegetation). These should be further considered for inclusion in Australia's national accounting, and subsequent method development.

In regard to review of methods, we would suggest that methods that have very few or no registered projects should in fact be subjected to further review and/or public comment on a more, rather than less, frequent basis. For example, if there are no project registrations under a method within one year of release there could be a request

[1] https://ic.fsc.org/en/what-is-fsc-certification/principles-criteria/fscs-10-principles

for public comment to understand the reason for low uptake. The rationale for early or more frequent review is to determine why there has been no or limited uptake in order to assess whether there are any readily available amendments to the method that would facilitate greater uptake. These could include changes to eligibility or more substantive criteria that would not adversely impact abatement outcomes or integrity.

In terms of new method development, we also suggest that there are opportunities for efficiency gains. While Climate Friendly understands the need for close government involvement to ensure technical proposals are translated into high quality legal drafting, the current process does not sufficiently draw on the respective strengths of government, project developers and academia. The Department of Environment and Energy teams leading method development are highly consultative when a method reaches the stage of being reviewed by a technical working group, but there is little transparency or opportunity to input on what methods are selected and prioritised for development at the outset. This has the unfortunate outcome that some methods prioritised for development do not align with actual project potential on the ground, and similarly that good ideas for methods with widespread potential for uptake are not allocated sufficient government resources to enable them to be developed in a timely manner.

We suggest that more resources should be invested by the government to oversight method development, as this is essential to realise the abatement opportunities remaining across the country. Additionally, we suggest that there should be a well-structured process for submitting ideas on methods, including potentially a requirement for the proposer to prepare draft legislation, combined with a mechanism for recognising early action that delivers abatement under methods that are in-development. Given the timeframes for finalising a method are commonly in excess of two years based on current processes, this recognition of early action is essential to encourage continued innovation and investment.

2. Permanence: question 11, 12, 13

In relation to the vegetation regrowth methods, Climate Friendly believes that in the absence of additional incentives to retain forest cover, there is significant risk that many proponents will revert to historical suppression activities at the end of their 25 year permanence period. In the absence of carbon finance, current economic incentives favour deforestation, as the percentage of forest canopy cover is inversely proportional to pasture growth.

To prevent a reversal of the atmospheric benefits achieved by the projects, we suggest four possible solutions (which can be undertaken in combination):

1) Project proponents undertaking sequestration projects should be allowed to vary projects with 25 year permanence periods to a project with 100 year permanence period at any point in the project crediting period. If the option to extend the permanence period is exercised, they should receive back-credit equivalent to the “buffer” ACCUs that were deducted from their ACCU issuances.
2) The crediting period for all reforestation projects could be extended from 25 years to at minimum match the permanence period, noting that credits from

reforestation start to taper off, although in some cases this may not be until years 40 to 50. Without enabling credits post year 25 there is very little incentive to go to a 100 year crediting period.

3) The Government could invest in local industries that provide a sustainable economic use for the forest at the end of the permanence period. For example, a bioenergy or other sustainable forest product industries.
4) Investigating options for other time frames of permanence (i.e. 40 years with a discount of 15%) may provide some flexibility which, coupled with point one, may enable proponents to test the market for the most suitable timeframe for their needs. Alternatives to longer permanence periods could include implementation of a scheme for rolling renewal of the 25 year permanence period. This 'atmospheric rent' model recognises that temporary removal of emissions from the atmosphere has value. This could involve an associated extension of the crediting period, or an alternate form of economic compensation, for example an interest-free loan in proportion to the amount of carbon stored in the Project Area.

3. Aggregations: question 15

Contract aggregations (as opposed to project aggregations) have been of central importance in enabling greater participation in land use methods. They provide a risk management tool, without which many landholders would be unable or unwilling to participate in the ERF. At a project scale, there are many seasonal variations and property management challenges that are beyond the control of landholders. These create significant risk for individual landholders to take on Carbon Abatement Contracts. Aggregations provide a tool to manage contractual obligations on a portfolio basis, similar to risk management services offered in other industries and sectors. As such, in our experience as a project developer, contract aggregations have been a critical tool underpinning the successful growth in project registrations and associated delivery of abatement under the ERF.

However, while contract aggregations have served as a useful risk management tool under the ERF relating to contractual obligations, there are continued challenges using project aggregation models in order to enable landholders with small land areas to participate in the scheme. This is owing to the extensive administrative processes (e.g. intense registration, eligible interest holder consent, reporting and audit processes) that are incurred in relation to each individual property. As a result, there are no real economies of scale that can support the aggregation of small landholdings to translate them into a commercially viable aggregated project. In order for project aggregations to better enable small-medium scale landholders to more readily participate in the ERF, there would need to be significant changes to scheme governance and administration to reduce the expenses associated with registering projects, obtaining consent, as well as simplified auditing and ongoing project reporting.

4. Indigenous Participation

Climate Friendly has established Memorandums of Understanding (MOU) with three Aboriginal Corporations relating to several Human-induced Regeneration projects in Queensland, with two more agreements currently under discussion. These agreements deliver significant commercial benefits to the involved Aboriginal Corporations. Benefits include revenue share, jobs, additional land access and assistance in undertaking cultural heritage surveys. They involved initial briefings to the Prescribed Body Corporate (PBC) Boards, joint site visits and formal Native Title Holder authorization meetings to finalise the commercial terms and provide the CFI EIHC Form for the project.

Additionally, Climate Friendly is a shareholder in Natural Carbon, a joint venture established in 2014 with a focus on developing savanna burning projects with Aboriginal communities in northern Australia. (Phillip Toyne, indigenous advocate, co-founder of the national Landcare program and founding Director of EcoFutures, was instrumental in the formation of Natural Carbon.) Since 2014, Natural Carbon has established itself as a leading organisation supporting savanna burning and Aboriginal carbon farming. This includes supporting the establishment of 10 savanna burning projects, including with the Pormpuraaw Aboriginal Shire Council, Olkola Aboriginal Corporation and Batavia Aboriginal Corporation.

Despite the above mentioned partnerships, we believe there are several barriers that continue to limit Indigenous participation in the CFI and ERF. Barriers include both the need for further training and skills development, as well as financial barriers, particularly during the start-up phase of projects. These financial hurdles could potentially be resolved through this project by the provision of a grant facility for establishment and management of projects, to assist to cover start-up implementation costs prior to first ACCU issuance. These costs typically include vegetation mapping and verification, fire management plan, early season burn operations; establishment of governance structures and costs of legal advice.

More broadly, Climate Friendly believes that best practice project development under the ERF involves active engagement with Native Title Holders (as opposed to fostering development of projects only on non-Indigenous lands). Best practice should not only be fully compliant legally, but should also deliver additional opportunities for partnerships and shared commercial benefits. Given the different land use methods and regional contexts under which these partnerships could be formed, we believe that a one-size fits all model will not work.

To this end, Climate Friendly is actively engaged with relevant Land Councils, state and federal government agencies and Indigenous service providers to support the development of frameworks for consultation, delivery of finance and formation of partnerships with Native Title Holders and other Indigenous stakeholders, with the goal of scaling up Indigenous participation in the ERF. This includes working together on high level principles around engagement with Native Titles Holders for inclusion in the Industry Code of Conduct that is under development, as well as more detailed industry guidance and templates for implementing these principles. We propose that this guidance is best developed on a method-specific and regional basis given the diversity of circumstances surrounding Indigenous participation.

5. Scheme Governance: various questions

Agency:

Project agents play an important role in facilitating participation in the ERF. Without agents, the vast majority of project proponents would be unable to navigate the scheme eligibility requirements and do not have the breadth of technical skills required to monitor and report on compliance with the method and related legislation. Carbon farming is not their core business, but a new sector which like any other industry requires specialised service providers. Assistance from agents who understand the detailed legal requirements, and who are specialised in project administration and technical methods, is essential to the success of the ERF.

Climate Friendly has over the past year co-chaired the Project Developers Council, which is working towards a Code of Conduct for the industry. We believe that best practice and accountability of agents is integral to the ongoing success of the ERF and are committed to delivering this across our own project portfolio.

The CFI legislation enables agents to assist project proponents in the administration of their project. Section 290 of the *Carbon Credits (Carbon Farming Initiative) Act 2011 (Cth)* (CFI Act) outlines some of the key actions that agents may undertake on behalf of project proponents of the scheme. In addition, it states that the broader "principles of agency" also apply. While Climate Friendly enjoys a very productive working relationship with the Regulator, during the course of scheme administration we have encountered some instances where we believe the provisions in this Section have been misinterpreted and the roles of agents and project proponents conflated. There are some instances where the Clean Energy Regulator will only accept sign-off or submissions directly from proponents, for example around audits. While it is clear that the audited body is the project proponent, based on legal advice Climate Friendly has received and our interpretation of the principles of agency in law, we believe that agents are empowered to manage project related actions on behalf of proponents, including but not limited to audits.

Alternatively, in other instances the Clean Energy Regulator has suggested that agents are responsible for the veracity of information that they pass on to the Regulator based on information supplied and instructions from project proponents. While Climate Friendly fully supports the need for agents to have robust due diligence processes to verify information that can readily be checked based on publicly available data, for example land ownership verified through land titles, we suggest that agents should not be responsible for the veracity of other information that they convey based on client instructions and have no capacity to verify. Rather, project proponents maintain direct responsibility for the veracity of such information provided to Climate Friendly and on-supplied to the Regulator on their behalf. Maintaining clear distinctions between the roles of agents and project proponents is imperative to both the operational efficiency and the ongoing integrity of the scheme.

Additionally, in the consultation paper you ask whether the Clean Energy Regulator should be entitled to see commercial terms between agents and project proponents. From Climate Friendly's perspective, these commercial terms are private contracts between the parties and should not be made available as a matter of course, while there may be some specific circumstances where it becomes appropriate for contractual arrangements to be shared in-confidence. They have no direct bearing on the

generation and crediting of carbon abatement. Rather, these standard commercial in-confidence arrangements are important to facilitate a viable long term carbon industry and associated deep, liquid carbon markets.

Administrative efficiency, transparency and guidance:

In terms of consistency in decision making, from time to time, Climate Friendly has sought advice from the Clean Energy Regulator, or where appropriate the Department of Environment and Energy, on their interpretation of certain aspects of the legislation or methodologies. Often their responses have widespread implications on our project portfolio, and potentially the scheme more broadly. Yet the responses are often informal and remain un-documented. This can create an unfair advantage, or inconsistency in implementation approaches, for market participants that have not received the same advice.

Climate Friendly suggests that the Clean Energy Regulator adopt a policy of documenting and then making available for comment all advice related to interpretation of the legislation and methodologies. Following a comment period, advice could then be formally published (in the form of 'Regulatory Advice'), and then communicated via the Regulator's email lists. We acknowledge that such a process could be lengthy, and therefore interim decision-making procedures would also be needed to enable project development to proceed, pending formalisation of the advice.

Project consents:

A number of challenges remain in terms of obtaining project consents. Consent requirements vary in every state, and in relation to every land tenure type. Consent holders, including financial institutions, all have their own unique processes and requirements. We continue to encounter new challenges in working with new interest holders who are unfamiliar with the ERF and/or do not have any processes for considering consent. These interest holders can vary from state governments, such as Western Australia who is only now considering its consent requirements, federal government departments who have interests in relation to particular methods (e.g. plantations) or areas of land (e.g. departments who manage telecommunication networks or energy pipelines), to Aboriginal Corporations who are being asked for consent as Native Title Holders, to financial institutions or individuals.

Given the breadth of different actors involved and the vary levels of capacity, administration or scheme familiarity, obtaining consents remains challenging. The time taken to obtain consent and, where relevant, associated commercial negotiations, can make projects unviable owing to legislative deadlines or commercial feasibility.

While we understand the importance of consent, we consider that simplified forms and potentially even more targeted criteria for what constitutes an interest holder, as well as active engagement from the Australian Government with other state and territory governments would assist in improving efficiencies in obtaining project consents.

Project audits:

In relation to project audits, Climate Friendly is supportive of the risk-based approach to auditing, whereby audits are obtained at specified intervals throughout the project lifetime, rather than every time ACCUs are created.

We note that, over time, auditing requirements have become more detailed. In general, we are supportive of this, as scheme integrity is of the utmost importance to all participants to ensure the longevity of the industry and that abatement is real. However, at times this goes beyond issues that have any material impact on the scheme. To ensure processes continue to remain streamlined, effective and efficient, it is imperative that audit requirements do not extend beyond material issues. Over-audit of projects risks the commercial viability and will likely impact continued uptake of the scheme.

Project applications & online systems:

While the Clean Energy Regulator has undertaken significant work to automate forms in the ERF Portal, we encourage further work on these systems.

There remain numerous system glitches, including differences between questions that appear in the portal and those that appear in printed versions of the portal form. Further, Climate Friendly regularly encounters problems with projects that we manage not appearing in the portal, which takes time and resources for both the Regulator and our organisation to resolve.

Additionally, we suggest that moving towards a shared project information base that provides visibility of the same project information to agents / project proponents and the Regulator would be very valuable. This could include real time information about applications, project start dates, pending deadlines, among other things. At present, information is organised by individual applications rather than by project. This results in significant duplication of effort in tracking projects within the Regulator and Climate Friendly, as well as for other project proponents or project developers. Having a shared information base would further reduce the risk that stakeholders are working off outdated information sets.

6. Markets and Pricing: various questions

The price of carbon remains a key factor limiting project uptake. A higher price for carbon through a market based system would better stimulate continued growth and increased abatement to contribute towards Australia's contribution to the Paris Agreement.

Climate Friendly is a member of the Carbon Market Institute (CMI) and supports the principles of a market based mechanism. In addition to increasing the array of available methods, as per our earlier comments, we also believe the other core benefits should be monetised to stimulate investment in projects that deliver not only carbon abatement, but other core benefits, including but not limited to socio-economic benefits to Indigenous communities and biodiversity benefits.

To ensure that ACCUs are eligible for future international markets, it is critical that methods are reviewed in the context of evolving international accounting rules and IPCC guidance. It is also critical that the Australia Government invests resources in updating inventory and accounting processes, so that we take full advantage of reporting on all available abatement opportunities in Australia that align with the international rules.

There are several areas in the land use inventory and accounting that could be further developed to expand the possible methods available.

Uncertainty around policy settings has a significant impact on investment in project design and innovation, as noted in our covering letter to this submission.