



AUSTRALIAN PETROLEUM PRODUCTION & EXPLORATION  
ASSOCIATION LIMITED

# REVIEW OF THE CARBON POLLUTION REDUCTION SCHEME WHITE PAPER

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APPEA Comments

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## 1. INTRODUCTION

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The Australian Petroleum Production & Exploration Association's (APPEA) comments are focussed on that part of your Terms of Reference dealing with the impact of the Government's proposed scheme, both with and without a global agreement to tackle climate change, on the liquefied natural gas (LNG) industry, as well as broader emissions trading scheme design issues of importance to the Australian upstream oil and gas industry.

In particular, APPEA comments are focussed on four issues:

- the role of LNG as a 'cleaner global contributor' and as an 'anomaly';
- the potential impact of the domestic emissions trading scheme on the LNG industry: modelling by Concept Economics;
- treatment of unincorporated joint ventures; and
- the expanded Renewable Energy Target.

In addition to the APPEA submission, a number of APPEA members have made individual submissions to you commenting on the White Paper. APPEA commends these to you.

## 2. THE ROLE OF LIQUEFIED NATURAL GAS AS A 'CLEANER GLOBAL CONTRIBUTOR'

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LNG has been characterised as an 'anomaly', whose characteristics – whilst the production of LNG is emissions intensive and adds to greenhouse gas emissions in Australia, natural gas, as will be considered further below, makes a substantial contribution to reducing global greenhouse gas emissions – must be recognised and accommodated in the design of a domestic emissions trading scheme.

This means that the LNG industry is not easily accommodated within the emissions-intensive trade-exposed framework set out in White Paper and implies that an alternative policy approach may be required. This alternative – the 'Clean Global Contributor' mechanism – is considered further below.

APPEA noted in its submission to the Carbon Pollution Reduction Scheme Green Paper<sup>1</sup> and to the Senate Select Committee on Fuel and Energy<sup>2</sup> that it would be unfortunate if, by unnecessarily constraining Australia's LNG industry, the design of the emissions trading scheme were inadvertently to

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<sup>1</sup> APPEA's submission to the Carbon Pollution Reduction Scheme Green Paper can be found at [www.climatechange.gov.au/greenpaper/consultation/pubs/0834-appea.pdf](http://www.climatechange.gov.au/greenpaper/consultation/pubs/0834-appea.pdf).

<sup>2</sup> APPEA's submissions to the Senate Select Committee on Fuel and Energy can be found at [www.aph.gov.au/Senate/committee/fuelenergy\\_ctte/submissions/Sub0018.pdf](http://www.aph.gov.au/Senate/committee/fuelenergy_ctte/submissions/Sub0018.pdf), [www.aph.gov.au/Senate/committee/fuelenergy\\_ctte/submissions/sub0018a.pdf](http://www.aph.gov.au/Senate/committee/fuelenergy_ctte/submissions/sub0018a.pdf) and [www.aph.gov.au/Senate/committee/fuelenergy\\_ctte/submissions/sub0018b.pdf](http://www.aph.gov.au/Senate/committee/fuelenergy_ctte/submissions/sub0018b.pdf).

undermine the scheme's ultimate objective of helping the world to reduce greenhouse gas emissions.

In this respect, the White Paper has amended the proposed treatment of emissions-intensive trade-exposed (EITE) activities, as set out in Policy Position 12.10 on page 12-47, compared to that proposed in the Green Paper. A potential implication of this change is that, provided it meets the criteria set out in the White Paper (formal emissions-intensity and trade-exposure assessments), LNG may qualify for an allocation of permits (compared to the proposal in the Green Paper, under which LNG would not have qualified for any permit allocation).

This implies that the adverse impacts on the Australian LNG industry may be somewhat lessened by White Paper's policy position compared to that proposed under the Green Paper. It remains the case, however, that the industry will face a significant cost impact not faced by its competitors and customers and that the growth and development prospects of the Australian LNG industry will be adversely impacted as a direct result.

A fundamental principle in designing a domestic emissions trading scheme in the absence of a global scheme must be to ensure that it produces similar production and investment outcomes to those reasonably expected under a global scheme. With that in mind, APPEA is particularly concerned that the rationale for permit allocation to EITE activities has been altered from the Green Paper to the White Paper to remove the consideration of the extent to which industries would expand under a global carbon constraint, and contribute to reducing global greenhouse gas emissions. Subjected to a global price of carbon, the natural gas industry could be expected to grow, as a consequence of having 50 to 70 per cent fewer emissions when used in electricity generation compared to a coal alternative. Yet, the domestic scheme as proposed would see its growth potential constrained.

There is a global environmental benefit to encouraging the expansion of the natural gas industry, including 'cleaner global contributors' like Australian LNG. Under a global carbon constraint, natural gas and the LNG industry could be expected to expand and Australia could play a key role in that global growth. The White Paper however, does not recognise the potential of domestic gas and fails to recognise cleaner global contributors, particularly LNG, when contemplating national and international reduction targets.

In summary (and while there may be different ways of achieving this), the industry continues to believe that there is a compelling case for not having the Australian LNG industry bear any additional cost impact for as long as our competitors and customers are not subject to a similar impost.

One of the possible ways to achieve this outcome advocated by APPEA as part of our response to the Green Paper, was the recognition of LNG and potentially other eligible activities, as a cleaner global contributor. APPEA proposed this be included within the emissions trading as a transitional

measure to operate in the absence of an international carbon price on Australian LNG competitor and customer countries.

The proposed mechanism encompassed the following criteria to assess cleaner global contributor activities and therefore determine eligibility:

1. Global contributor: emissions reduced globally as a consequence of the product are more than the associated emissions produced in Australia;
2. Global sustainability: industry would expand under a global carbon price;
3. Affordability: economic benefit to Australia through additional taxation revenue associated with the industry's expansion would exceed the cost to Government; and
4. Trade exposed: capacity for passing through costs is restricted as a consequence of both competitor advantages and the substitutability of cheaper alternatives in the absence of a global carbon price.

A cleaner global contributor mechanism would offset international competitive disadvantage through the grant of permits representing the total of their direct and indirect emissions. Other measures of corresponding value could also be considered as a means for delivering a 'no net cost' outcome.

Further details of the cleaner global contributor mechanism can be found at **Attachment 1**.

## **2.1 The potential impact on the liquefied natural gas industry: modelling by Concept Economics**

On 24 September 2008, APPEA released analysis of the impact on Australia's LNG growth potential of a domestic emissions trading scheme operating in the absence of a broad global scheme<sup>3</sup>.

The analysis, conducted by independent economic consultants Concept Economics, drawing on an Access Economics model, examined the impact of the Government's preferred position as outlined in the Green Paper on the Australian economy and on the Australian LNG industry under three scenarios.

The analysis shows that in a situation where Australia unilaterally commits to a reduction in greenhouse gas emissions of 20 per cent on 2000 levels by 2020 (on the way to a reduction of 60 per cent by 2050), the impact on

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<sup>3</sup> The Concept Economics report, *Estimated Impacts of the Proposed Domestic Emissions Trading Scheme on the Oil And Gas Industry*, can be found at [www.appea.com.au/content/pdfs\\_docs\\_xls/NewsMedia/APPEAMediaReleases/appea\\_ets\\_report\\_23\\_sep\\_08\\_2.pdf](http://www.appea.com.au/content/pdfs_docs_xls/NewsMedia/APPEAMediaReleases/appea_ets_report_23_sep_08_2.pdf) and the associated media release launching the report, "Liquefied Natural Gas Carbon Modelling Released", can be found at [www.appea.com.au/content/pdfs\\_docs\\_xls/NewsMedia/APPEAMediaReleases/ets\\_modelling\\_mr\\_2409\\_08\\_2.pdf](http://www.appea.com.au/content/pdfs_docs_xls/NewsMedia/APPEAMediaReleases/ets_modelling_mr_2409_08_2.pdf).

LNG is severe, with output in the industry falling by more than 37 per cent in 2020 and more than 54 per cent in 2030 compared to what it otherwise would have done. In a scenario where emissions in 2020 are the same as those in 2000 (on the way to a reduction of 60 per cent by 2050), LNG output falls by 16 per cent in 2020 and more than 34 per cent compared to what it otherwise would have done.

While this modeling was conducted in the context of the Green Paper's proposals and not the White Paper's policy positions, as the recently released peer review of the Treasury modelling of the economic impacts of reducing emissions<sup>4</sup> notes, on pages 29-30

*The impact of an ETS on the LNG industry is likely to be significant for two reasons. First, both the production of gas and the processes required to transport LNG are emissions-intensive. In addition, LNG projects are highly capital intensive and changes in costs, such as those imposed by an ETS, are enough to make many projects unviable.*

*Modelling work by Concept Economics suggests that under plausible ETS scenarios LNG output is likely to be between a third and a half less than it otherwise would be by 2030. This is the case regardless of whether or not the government offers to shield the industry with assistance for a period of time. This is based on a study of trajectories which span the two CPRS scenarios (0, 10 and 20 per cent reductions by 2020), but with more realistic international action and permit trading assumptions.*

*While 60 per cent permit allocation lessens the competitive impact on the industry, output would still be between 16 and 37 per cent below the reference case level in 2020, and between 39 and 54 per cent down on what it otherwise would be by 2030. Broadly similar results are reported for natural gas.*

In relation to the broader issue of economic modelling of the impacts of an emissions trading scheme, APPEA notes the Concept Economics peer review made a number of recommendations based on its analysis of the Treasury modelling, and set these out on page 5 of the Concept Economics report. APPEA endorses these recommendations.

### **3. TREATMENT OF UNINCORPORATED JOINT VENTURES**

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Operations within the upstream oil and gas industry are generally undertaken within unincorporated joint ventures (UJVs). These structures, which are typical world-wide, provide entities with the opportunity to spread risk across a portfolio of activities, allow funding to be derived from

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<sup>4</sup> This review, conducted by Concept Economics, *A Peer Review of the Treasury Modelling of the Economic Impacts of Reducing Emissions*, was commissioned by the Senate Select Committee on Fuel and Energy. A copy can be found at [www.aph.gov.au/Senate/committee/fuelenergy\\_ctte/senate\\_ets\\_report\\_020209\\_final.pdf](http://www.aph.gov.au/Senate/committee/fuelenergy_ctte/senate_ets_report_020209_final.pdf).

a range of sources and allow expertise to be drawn from the different parties within a single project.

APPEA recommended, in its submission to the Green Paper, that participants with projects/activities being undertaken within unincorporated joint ventures be provided with flexibility in meeting their greenhouse obligations to ensure that any final measures are complementary to the legal and commercial framework within which these structures operate.

APPEA acknowledges that, in the case of UJVs, the White Paper, in Policy Position 7.7 on page 7-9, has better recognised the need for flexibility for determining liabilities for acquittal of permits than did the Green Paper's preferred position. Policy Position 7.7 establishes:

*The participants to unincorporated joint venture agreements will be free to break up the task and cost of purchasing compliance permits according to their specific agreements, with the entity with operational control being finally liable to surrender the correct number of compliance units for the covered facility<sup>5</sup>.*

While the White Paper's Policy Position is an improvement, APPEA seeks to further increase flexibility with regard to the acquittal of permits by unincorporated joint ventures. APPEA recommends the Policy Position adopted read as follows:

*The participants to unincorporated joint venture agreements will be free to break up the task and cost of purchasing compliance permits according to their specific agreements, with each participant being finally liable to surrender the correct number of compliance units for the covered facility according to their specific agreement.*

### **3. RENEWABLE ENERGY TARGET**

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The Government, both directly through the release of exposure draft legislation in December 2008, and in the White Paper, has continued the development of a Renewable Energy Target (RET) as a so-called complementary measure, noting that

*renewable energy will have a key role in moving Australia to the clean economy of the future. The Renewable Energy Target (RET) will ensure that 20 per cent of our electricity is generated from renewable sources by 2020<sup>6</sup>.*

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<sup>5</sup> Australian Government (2008), *Carbon Pollution Reduction Scheme, Australia's Low Pollution Future*, White Paper, Chapter 7, Policy Position 7.7, December, p. 7-9 (available at [www.climatechange.gov.au/whitepaper/report/index.html](http://www.climatechange.gov.au/whitepaper/report/index.html)).

<sup>6</sup> Australian Government (2008), *Carbon Pollution Reduction Scheme: Australia's Low Pollution Future*, Chapter 19, p. 19-4.

As APPEA noted in our submission to the Green Paper and to the Government on the various RET-related consultations<sup>7</sup>, the RET does not represent an efficient or cost effective greenhouse policy response. As APPEA's submission noted, work commissioned by APPEA from respected global economic consultants CRA International found that a renewable energy target introduced alongside an emissions trading scheme is significantly less efficient than an emissions trading scheme alone in achieving a given level of emissions abatement<sup>8</sup>.

Of particular concern is the White Paper's lack of rigorous assessment of the cost effectiveness of the RET scheme and a lack of formal justification of the RET against the Government's own principles, as outlined in Policy Position 19.1 on page 19-4 and agreed amongst all jurisdictions as part of the *COAG Principles for Jurisdictions to Review and Streamline their Existing Climate Change Mitigation Measures*<sup>9</sup>.

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<sup>7</sup> A copy of APPEA submission to the COAG Working Group on Climate Change and Water on its consultation paper on the design of the RET scheme, *Design Options for the Expanded National Renewable Energy Target Scheme*, is available at [www.climatechange.gov.au/renewabletarget/consultation/pubs/012apia.pdf](http://www.climatechange.gov.au/renewabletarget/consultation/pubs/012apia.pdf).

<sup>8</sup> A copy of the CRA International report, *Implications of a 20 per cent renewable energy target for electricity generation*, is available at [www.garnautreview.org.au/CA25734E0016A131/WebObj/D0848328ETSSubmissionSupportingDoc-APPEA/\\$File/D08%2048328%20ETS%20Submission%20Supporting%20Doc%20-%20APPEA.pdf](http://www.garnautreview.org.au/CA25734E0016A131/WebObj/D0848328ETSSubmissionSupportingDoc-APPEA/$File/D08%2048328%20ETS%20Submission%20Supporting%20Doc%20-%20APPEA.pdf).

<sup>9</sup> These principles can be found at [www.coag.gov.au/coag\\_meeting\\_outcomes/2008-11-29/docs/20081129\\_complementarity\\_principles.pdf](http://www.coag.gov.au/coag_meeting_outcomes/2008-11-29/docs/20081129_complementarity_principles.pdf).

