

# THE 6<sup>TH</sup> SEMINAR ON ENVIRONMENTAL AUDITING AND 5<sup>TH</sup> WORKING GROUP MEETING OF ASOSAI WGEA



## Country Paper: Australia

### Theme: Implementation of Environmental Policy

### *Performance Audit: Abatement Crediting and Purchasing under the Emissions Reduction Fund*



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Jaipur, India

## Background information

In November 2014, the Australian Government established the Emissions Reduction Fund—a voluntary scheme that allows participants (including farmers and industrial companies) to earn carbon credit units by implementing projects they propose that abate carbon.<sup>1</sup> Through reverse auctions, the Government then purchases from willing sellers a proportion of the carbon credit units already earned or expected to be earned in the future by registered projects. The government-purchased carbon credit units (once earned by the projects and transferred to the government) are used to meet Australia's greenhouse gas emission targets under the Kyoto Protocol. Carbon credit units not purchased can be sold on the secondary market to enable other entities to meet their carbon abatement obligations.

The Emissions Reduction Fund is administered by the Clean Energy Regulator (a government statutory authority) that is responsible for (i) registering projects that apply an approved fund method; (ii) verifying the carbon abatement claims of projects before issuing carbon credit units; and (iii) purchasing carbon credit units from willing sellers through reverse auctions. A precursor to registering projects under the Emissions Reduction Fund is the development and approval of fund methods—a function that is undertaken by a separate government entity, the Department of the Environment and Energy—which outline eligibility requirements and the methodology for calculating the carbon abated by the projects. An overview of the fund's abatement crediting and purchasing components is provided in Figure 1 (on the following page).

Eligible projects can relate to activities that reduce/avoid greenhouse gas emissions or increase carbon stores from:

- agricultural activities
- reforestation, revegetation or protecting native forest/vegetation
- carbon sequestration
- controlled burning activities
- energy efficiency
- landfill and alternative waste treatment
- mining, oil and gas
- transportation.

As at 1 July 2016, the regulator reported that it had registered 626 fund projects, 236 of which had been credited with a total of 25.4 million carbon credit units.<sup>2</sup> To date, the regulator has conducted three auctions (of which the first two were examined in the audit) and contracted to purchase 143.3 million carbon credit units over the next 10-12 years from successful bidders at a cost of AUD1.7 billion. Carbon credit units have been purchased at the first, second and third auctions at an average price of AUD13.95 per tonne, AUD12.25 per tonne, and AUD10.23 per tonne respectively.

## Importance of the topic

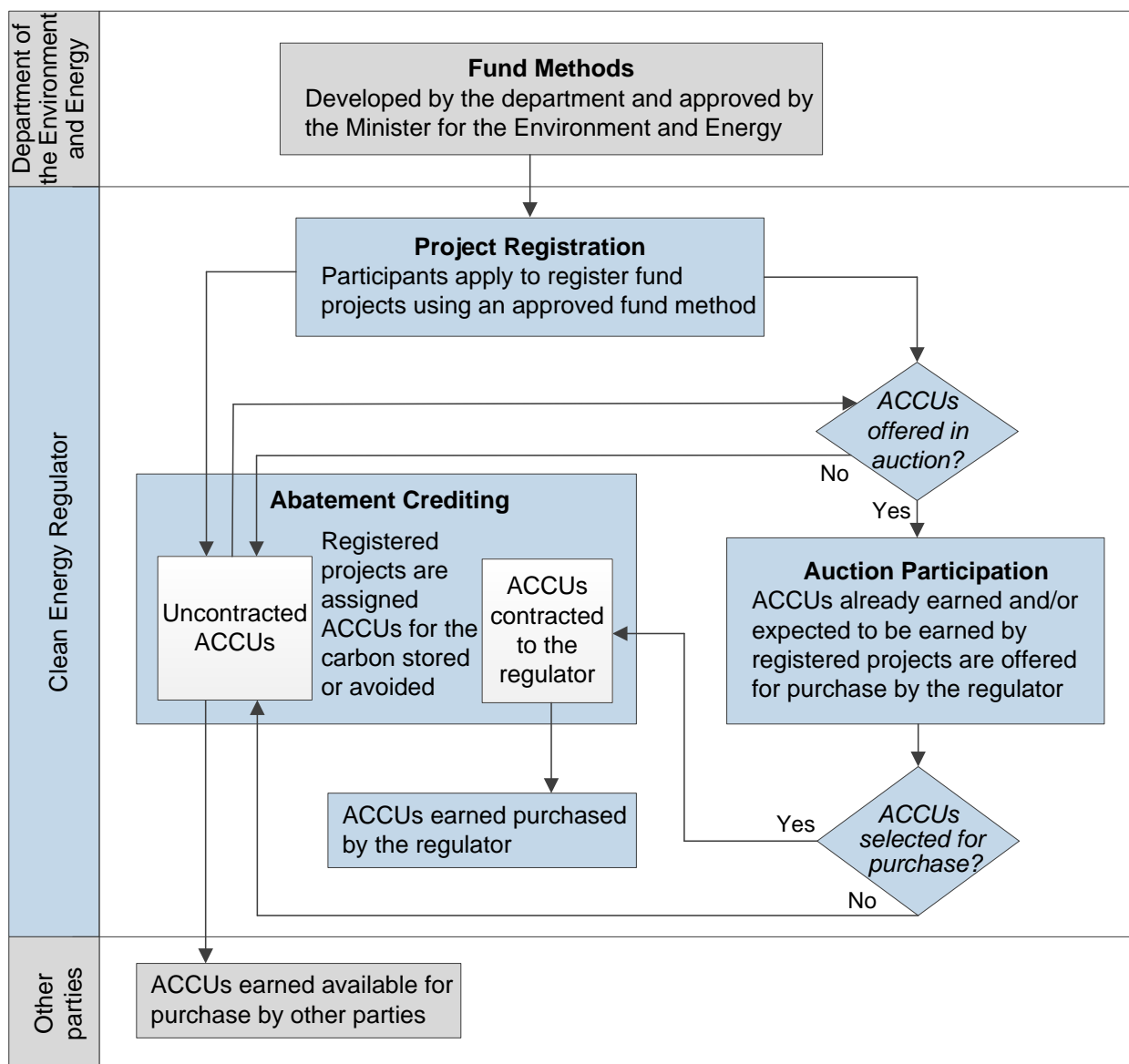
The fund is one of the primary mechanisms that Australia is using to achieve its greenhouse gas emissions reduction targets, with AUD2.55 billion having been allocated by the Government for the purchase of carbon credit units. The fund is expected to contribute an estimated 92 million tonnes of carbon dioxide equivalent towards Australia's 2020 cumulative carbon abatement target (with additional contributions expected towards Australia's 2030 carbon abatement target).

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<sup>1</sup> Carbon abatement projects registered under an earlier scheme, the Carbon Farming Initiative, transitioned automatically to the Emissions Reduction Fund.

<sup>2</sup> One carbon credit unit equates to one tonne of carbon dioxide equivalent (1 tCO<sub>2</sub>-e) of abatement.

**Figure 1: Overview of the fund's abatement crediting and purchasing components**



ACCUs – Australian Carbon Credit Units.

## Audit Objectives

The objective of the audit was to assess the effectiveness of the Clean Energy Regulator's crediting and selection of carbon abatement to purchase under the Emissions Reduction Fund. To form a conclusion against this objective, the ANAO adopted the following high-level criteria:

- Did the regulator only register projects that met relevant legislative requirements?
- Did the regulator issue the correct quantity of carbon credit units to registered projects after verifying the claims from project proponents?
- Did the regulator design and implement the first and second auctions to purchase carbon credit units from eligible projects at least cost?
- Did the regulator appropriately manage the risks, operation and performance of the abatement crediting and purchasing components of the fund?

## Audit methods

The audit examined the regulator's administration of projects in relation to their registration, abatement crediting and participation in the first two auctions by examining a 10 per cent sample of the respective populations. In conducting the audit, the ANAO examined regulator records relating to the administration of the fund, including standard operating procedures,

assessment tools, implementation strategies and plans, and other governance documentation. The ANAO also interviewed regulator staff and sought comments on the regulator's administration of the fund from project proponents and peak industry groups.

## **Result of the audit**

### ***Overall conclusion***

The audit concluded that Clean Energy Regulator had established sound arrangements to manage the crediting and selection of carbon abatement for purchase under the Emissions Reduction Fund. There were some aspects of the regulatory process that, nonetheless, required further attention—such as the level of documentation underpinning some areas of regulatory decision-making—to enable the regulator to better demonstrate the effectiveness of its regulatory activities.

### ***Key findings***

- Applications for fund project registration and variation had been effectively assessed by the regulator, but documentation of some regulatory processes and decisions could be improved. The regulator had, in the main, applied sound processes to approve, declare and register fund projects in accordance with legislated timeframes. The decision minutes, while reflecting accurately the assessments undertaken, did not always contain all information relevant to the assessment process.
- Appropriate arrangements were in place to assess the carbon abatement claims of fund projects against fund method requirements. Nevertheless, the justification for, and documentation supporting, streamlined routine assessments (determined on a risk basis) required improvement to enable the regulator to demonstrate the robustness of these assessments. Where the delegate approved the projects' carbon abatement applications, carbon credit units assigned to projects were accurately calculated according to fund method requirements and recorded in public registers.
- Within the context of the legislated purchasing principles of the fund, the regulator effectively designed the auction methodology, parameters and delivery arrangements for the first two carbon abatement auctions that were examined in the audit. Overall, the first and second auctions were conducted effectively and in accordance with published auction guidance. The regulator selected the least-cost abatement to purchase within the established auction parameters. The fulfilment of carbon abatement contracts will be dependent on the satisfaction of conditions precedent, the abatement credited to the projects over time and the effectiveness of the 'make good' provisions of the contracts.
- The regulator has a well-established and integrated risk management framework to guide the development and implementation of risk management plans for the fund. Under this framework, the regulator had established sound processes to identify, assess and treat risks to the effective implementation of the fund. The regulator has developed appropriate guidance, including standard operating procedures, work instructions and templates, to assist staff to assess fund applications. The regulator has an established performance management framework to monitor and report on fund performance, with work to strengthen the framework undertaken over recent years.

Further information regarding the audit's findings and conclusions can be found at: <https://www.anao.gov.au/work/performance-audit/emissions-reduction-fund-abatement-crediting-and-purchasing>.

### ***Recommendation***

The ANAO made one recommendation aimed at improving the Clean Energy Regulator's routine assessments of projects' carbon abatement applications.

## **Summary of entity response**

The Clean Energy Regulator agreed to the recommendation.

## **Experiences and challenges**

The audit provided the Australian Parliament with an assessment of the effectiveness of arrangements: (i) to recognise the carbon abated by projects when applying approved methods; and (ii) for the Government to purchase the projects' carbon abatement at least cost as a contribution towards Australia's greenhouse gas emissions reduction targets.

The ANAO experienced challenges in three particular areas:

### **1. Technical nature of the subject matter**

The Emissions Reduction Fund involved a number of technical processes. The audit team invested time early in the audit to meet with Clean Energy Regulator staff and review material early in the audit to build an understanding of these processes.

The technical nature of the subject matter also influenced the design of the audit test programs. The test programs were detailed so that technical matters of importance could be broken down into discrete processes allowing the testing to be repeated consistently for similar transactions. As testing progressed, test programs were modified and enhanced. The initial development and refinement of the detailed test programs was time-consuming, but a valuable audit investment that led to strong audit findings that supported our overall audit conclusion.

### **2. Sampling methodology**

The ANAO summarised the respective populations of registration, crediting and auction applications using their key parameters (such as, date of application submission, project method type, application assessor name, decision delegate name and assessment result). The ANAO then selected a 10 per cent sample broadly in proportion with the key parameters of the populations. The ANAO considered over a dozen key parameters when selecting the sample of project registrations and abatement crediting applications so that the sample selected closely resembled the characteristics of the respective populations. In this way, the ANAO was able to 'project' the audit findings from the sample examined to the respective populations.

### **3. Communicating audit results accurately and succinctly**

The technical nature of the audit subject matter and key concepts regarding the Emissions Reduction Fund, posed challenges for the ANAO to communicate the audit results accurately and succinctly to an external audience (including Parliamentarians, the media and general public). To the greatest extent practicable, the audit report avoided the use of technical terms, expression and jargon (or where these were necessary, they were described in plain language). The proposed audit report was also circulated within the auditee in advance of the finalisation of the audit to ensure that the operations of the Emissions Reduction Fund had been accurately described.

Other techniques used by the ANAO to communicate the operations of the Emissions Reduction Fund and audit findings and conclusions included the use of:

- diagrams (including Figure 1 above) to illustrate processes;
- a question and answer presentation approach to address the detailed audit criteria; and
- summary boxes that succinctly concluded against each audit criterion, with additional information provided to indicate the testing undertaken to address each audit criterion.