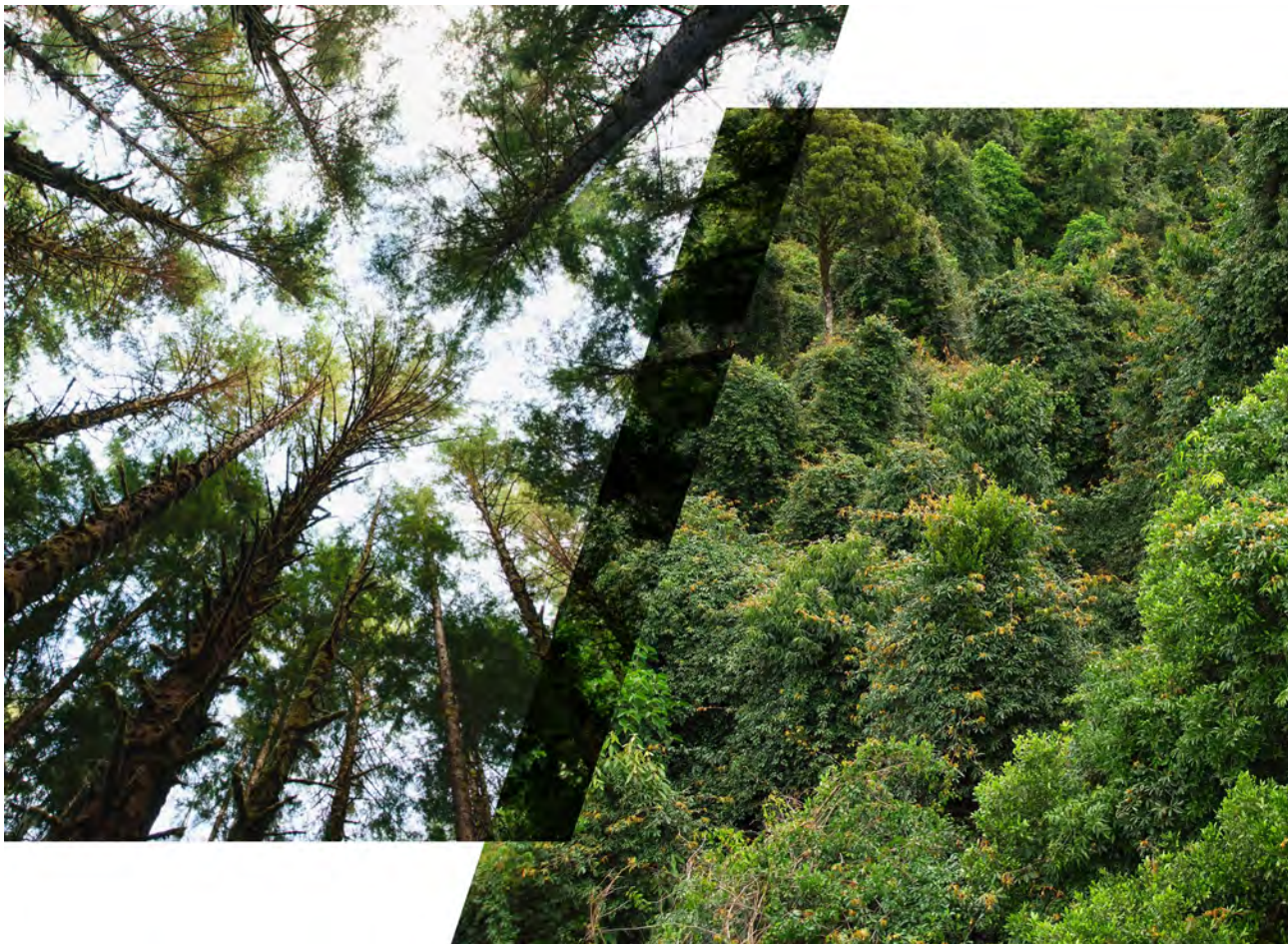


COP21:
Key implications
for business in Australia



With the historic Paris Climate Agreement in place - the legacy of intense global negotiations at the 21st Conference of Parties ('COP21') - 196 nations have now agreed to work together to curb increases in global average temperatures to well below 2°C above pre-industrial levels and to reach zero net global greenhouse gas emissions by the end of the century¹.

¹ Formal ratification of the Paris Climate Agreement is set to commence on 22 April 2016.

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The ink in the Paris Climate Agreement is barely dry, but attention has now turned to focussing on how these ambitious goals will be achieved. An important part of this equation will be the roles played by both the private and public sectors in translating these goals into reality. As it has been widely touted – the real work starts now.

With this Agreement as the backdrop, there are a number of key questions of particular relevance to the Australian business community which will need to be addressed over the coming weeks and months to provide the necessary clarity on the trajectory of Australia's transition to a clean energy economy. These questions include:

- What sense of urgency are we likely to see from Government around introducing or amending policies and regulations to meet these commitments?
- What are the prospects for the pricing of carbon and market mechanisms in Australia?
- How should business be proactively preparing for such changes?
- What does the future landscape for the Asia-Pacific renewable energy sector look like? How can business tap into this opportunity?
- What does the transition to carbon neutrality mean for Australia's traditional fossil fuel sector?
- How can Government and business support local communities that will be impacted by climate change regulation?

Over the following pages we provide an initial analysis on the factors shaping the answers to these questions.

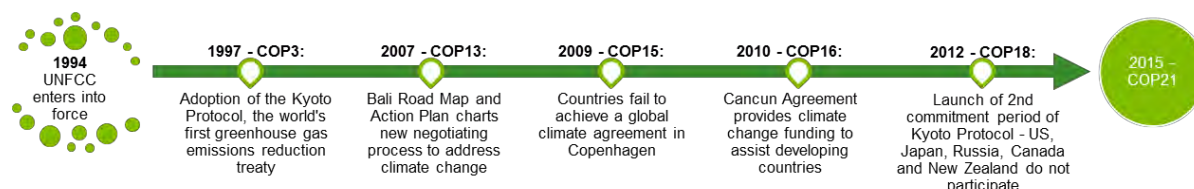


Figure 1: Climate milestones leading into COP21

Spotlight 1: Recap of highlights from the Paris Climate Agreement

- **Limiting global warming:** the Agreement includes an absolute commitment to limit increases in global average temperature to well below 2°C above pre-industrial levels and a further commitment to pursue efforts to limit the temperature increase to 1.5°C – recognising that a cap of 1.5°C would significantly reduce the risks and impacts of climate change. It is noted that the Intended Nationally Determined Contributions (INDCs), which have been submitted by over 180 countries to date, have been recognised under the Agreement but are not legally binding.
- **Peaking global emissions:** the Agreement outlines the aim to reach global peaking of emissions “as soon as possible”, with the recognition that peaking for developing country Parties will take longer.
- **Transparency is key:** transparency on the progress made by countries on meeting the emissions reduction commitments set out in their respective INDCs has been recognised as a critical step to achieving the goals set out in the Agreement and enhancing global cooperation on climate action. Countries will be required to submit nationally determined contributions every five years from 2018 (Article 4 (9)) and the global stocktakes will take place on this schedule from 2023.
- **Conservation of forests:** the Agreement recognises the importance that forests play in offsetting detrimental human-induced actions on the environment and encourages countries to enact policies developed over the last decade to preserve the world's remaining intact forests.
- **Climate finance assistance for developing countries:** developed countries Party to the Agreement are encouraged to take the lead in mobilising climate finance to support developing country Parties in climate adaptation and transitioning to clean energy economies. However, the goal of mobilising funds of at least US\$100 billion per year is not legally binding. This has been met with disappointment by many developing and smaller countries.

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Future direction of Australia's climate policy

Australia's current emissions reduction policy is centred on the Direct Action Plan ('DAP'), the centrepiece being the Emissions Reduction Fund ('ERF'), which aims to efficiently and effectively source low cost emissions reductions. Two ERF auctions have been held thus far, leading to a portfolio of carbon abatement controls that are scheduled to deliver almost 92.8 million tonnes of abatement at an average price of \$13.12 per tonne of abatement.²

Another key aspect of the DAP is the Safeguarding Mechanism which is designed to ensure that large emitting facilities keep their net emissions below a specified baseline, while also preventing emissions reductions purchased through the ERF being displaced by increased emissions elsewhere in the economy. The Safeguarding Mechanism is scheduled to commence on 1 July 2016, and will cover all facilities that emit over 100,000 tCO₂-e per year.

Australia's new climate commitments as outlined during COP21 include the following:

- An economy-wide target reduction in emissions by 26-28 per cent below 2005 levels by 2030
- A pledge of \$1 billion per year to the Green Climate Fund run by the United Nations to assist neighbouring developing nations with shifting to clean energy.

Australia's emissions reduction commitment has already been subject to critique, with some commentators and analysts arguing that Australia should be aiming for a more ambitious commitment. Likewise, Australia's climate aid pledge has also come under fire with some arguing that Australia should be doing more to help its regional, developing counterparts. The Agreement and the five yearly global stocktake processes are likely to lead to Australia coming under further pressure to increase this commitment.

It remains to be seen whether Australia's current approach to climate change mitigation and adaptation is likely to undergo significant development in order to meet the above mentioned commitments. The DAP, including the ERF, is scheduled for review in 2017. This review is set to consider whether current policies are sufficient to enable Australia to meet its emissions reductions targets under the Agreement.



Figure 2: Roadmap post COP21

Carbon market mechanisms – back in vogue?

Australia recently signed a Paris declaration calling for new clear rules for international carbon trading, with recognition that "it was in Australia's interests to recognise the role that an international carbon market might play in reducing emissions after 2020".³

There have also been discussions around the possibility of Australia allowing international carbon units to complement domestic measures to achieve our future commitments.

As highlighted by the Australian Government's Climate Change Authority, provided that the

The DAP, including the ERF, is scheduled for review in 2017. This review is set to consider whether current policies are sufficient to enable Australia to meet its emissions reductions targets under the Agreement.

² Clean Energy Regulator (2015), 'Average price of \$12.25 secures over 45 million tonnes of abatement at second auction', 12 November, available at: <http://www.cleanenergyregulator.gov.au/ERF/Pages/News%20and%20updates/News-item.aspx?ListId=19b4efbb-6f5d-4637-94c4-121c1f96fcfe&ItemId=188>

³ Taylor, L. (2015), 'Australia signs up for clear carbon trading rules, hinting at policy change', 10 December, available at: <http://www.theguardian.com/australia-news/2015/dec/10/australia-signs-up-clear-carbon-trading-rules-hinting-policy-change>

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underlying emissions reductions are genuine, they have the same impact on global climate outcomes as domestic emissions reductions.⁴ International trade in emissions reductions can also support the introduction of stronger targets where it may not be cost effective to do so solely through domestic actions. Should this occur it will mean that carbon market mechanisms are likely to play more of a role. Whether there are international linkages to an enhanced Safeguard Mechanism or another form of emissions trading scheme will be something to watch.

Business is also taking proactive steps to consider the implications of carbon on their operations through use of internal carbon pricing based on international and domestic considerations. A growing number of large organisations including many Australian organisations have signed up to the We Mean Business coalition⁵ which includes putting a price on carbon as a key commitment. We expect to see an increasingly number of Australian businesses adopting this practice in the short to medium term.

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Spotlight 2: What commitments have our regional counterparts made and what do they mean for Australia's economy?

In light of the interdependence of Australia's economy with our regional counterparts, commitments made by these countries to reduce the emissions intensities of their economies in the coming years present both risks and opportunities to Australian business.

While demand for fossil fuel exports is expected to decrease over time, renewable energy commitments made by Japan, China and Indonesia of 22%, 20% and 23% of total energy consumption by 2030, respectively, will provide significant market opportunities.

Country	Reduction commitment ⁶	Unit	Baseline year	Target year	Scope
Australia	26-28%	Absolute GHG	2005	2030	Economy-wide
New Zealand	30%	Absolute GHG	2005	2030	Economy-wide
China	60-65%	CO ₂ per unit GDP	2005	2030	Not specified
Japan	26%	Absolute GHG	FY 2013	FY 2030	Economy-wide
Indonesia	26%	Absolute GHG	BAU scenario	2020	Nationwide
Singapore	36%	GHG per unit GDP	2005	2030	Economy-wide

Table 1: Snap shot of Asia-Pacific INDCs

Increased focus on transparency

We are already seeing increased transparency on the corporate management of climate-related risks and opportunities. This is highlighted by the recent changes to environmental, social and governance ('ESG') disclosure requirements by regional Stock Exchanges including in Hong Kong and Singapore, which are in the process of transitioning to "if not, why not" regimes consistent with the approach adopted in Australia. Other examples include the publishing of portfolio risk analyses, particularly in the extractive sector.

From a government perspective, in order to meet the transparency requirements in the Agreement, countries will need to ensure that they have robust measurement and reporting frameworks in place. Australia's National Greenhouse and Energy Reporting ('NGER') scheme, which has been in place since 2009, is one of the world's leading national frameworks. As such, it is expected that Australia is well positioned to respond to these COP21 requirements. The NGER data will remain a vital source of truth for determining Australian's emissions profile now and into the future. In addition, with the commencement of the Safeguard Mechanism in 2016, the importance of the system for liable facilities will only increase.

With the move to more robust systems of global reporting, Australian companies with operations based overseas should prepare for potential additional emissions reporting requirements and look to leverage their Australian experience where possible.

⁴ Climate Change Authority (2014), Using International Units to Help Meet Australia's Emissions Reduction Targets: Research Report, July, available at: http://www.climatechangeauthority.gov.au/files/files/UIUHAERT/report_2.pdf

⁵ <http://www.wemeanbusinesscoalition.org/>

⁶ World Resources Institute, CAIT Climate Data Explorer, available at: <http://cait.wri.org/indc/>

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Innovation to take centre stage

Research and innovation are set to play an increasingly important role in addressing the diverse climate change issues facing Australia and the world more broadly. This was evidenced in Prime Minister Turnbull's announcement during COP21 that Australia will ratify the second commitment period to the Kyoto Protocol, with the statement including reference to innovation and technology as key enablers to achieving Australia's 2020 and 2030 emissions reduction targets to drive economic growth.⁷

Opportunity for renewable energy

Although some argue that Australia's approach to renewable energy investment has lacked the certainty and policy environment to enable long-term investments, there are growing signs that this is shifting. The recent green light provided to the Clean Energy Finance Corporation ('CEFC') to be able to consider wind projects again as part of the CEFCs \$10 billion fund⁸, coupled with commitments made to clean technology initiatives announced at COP21 including the Global Solar Alliance, Mission Innovation and the 4/1000 Initiative, indicate that the Turnbull Government is looking to make some serious strides in this direction.

The large scale uptake of renewable energy electricity and low emissions vehicles such as hybrid and plug-in electric vehicles, represent key enablers in Australia's transition to a low carbon economy. The availability of large, low cost, high capacity battery technology has been a significant prohibiting factor to date, however the tide is changing. Recent research highlights that battery costs have fallen on average by 14% annually between 2007 and 2014 and more significant cost reductions for lithium ion batteries are expected as several companies rapidly scale up production.⁹ With battery storage also expected to grow quickly, along with continued increases in electricity prices, electricity generation from renewable energy sources is expected to grow. Increased demand for electric cars stemming from improved battery storage capacity is also predicted over the medium to long term. According to the Climate Council, "half of all households in Australia are predicted to adopt solar systems with battery storage on the basis of a \$10,000 battery system with a payback of 10 years, with the market potentially growing to \$24 billion".¹⁰



Research and innovation are set to play an increasingly important role in addressing the diverse climate change issues facing Australia and the world more broadly.

The opportunities to business as a result of this impending shift are already becoming evident, with some large Australian companies starting to announce deals with leading global players such as Tesla to supply battery storage solutions to their customers.¹¹ We anticipate arrangements such as these will expand in light of the above mentioned trends and the introduction of further policy-driven incentives.

The importance of innovation to Australia's future economic and environmental prosperity comes at a time when innovation is also an increasingly critical theme for mining and resources companies since these industries are at a crossroads due to subdued pricing and changing macroeconomic factors. According to Deloitte's Tracking the trends 2016: Are we there yet?, "although today's lower cost of oil is reducing energy expenses for miners [and other resource companies], it's not likely to last. That's why forward-thinking companies continue to make strides towards the adoption of renewable energy alternatives. Numerous companies already generate wind, solar, hydro and biomass power supplemented by variable speed backup generators capable of maximising fuel efficiency; a solution that also works for companies running power off the grid.¹² As investment in clean technologies continues on both domestic and global fronts, the adoption of such practices is likely to become more widespread.

⁷ Turnbull, M. (2015), '2015 United Nations Climate Change Conference Speech', 1 December, available at: <http://www.malcolmturnbull.com.au/media/2015-united-nations-climate-change-conference-speech>

⁸ Keany, F. (2015), 'Federal Government lifts Tony Abbott's wind farm investment ban', ABC, 14 December, available at: <http://www.abc.net.au/news/2015-12-13/abbots-wind-farm-investment-ban-lifted/7024164>

⁹ Climate Council (2015), *Powerful Potential: Battery Storage for Renewable Energy and Electric Cars*, p. 11, available at: <https://www.climatecouncil.org.au/uploads/ebdfdf89a6ce85c4c19a5f6a78989d7.pdf>

¹⁰ Climate Council (2015), *Powerful Potential: Battery Storage for Renewable Energy and Electric Cars*, p. 11, available at: <https://www.climatecouncil.org.au/uploads/ebdfdf89a6ce85c4c19a5f6a78989d7.pdf>

¹¹ <http://www.smh.com.au/business/energy/origin-energy-snares-deal-with-tesla-to-sell-powerwall-battery-20151209-qli4lx.html> and <http://www.thefifthstate.com.au/business/investment-deals/csr-bradford-to-supply-tesla-powerwall-battery/79437>

¹² Deloitte (2016), *Tracking the Trends: Are we there yet?*, p. 13, available at: <http://www2.deloitte.com/ca/en/pages/international-business/articles/tracking-the-trends-2016.html>

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Whilst we think of global climate change, we must be mindful of the local impacts for communities

For developed economies such as Australia, there are further challenges and opportunities from a social perspective that are likely to arise from the transition to a low carbon economy. The first of these is the direct impact on communities in the form of jobs, particularly in the energy and extractive sectors. As the developed world transitions its energy mix away from fossil fuels, the regions that have supported these industries for generations will change. Regions such as the Latrobe or Hunter Valleys in Australia where thermal coal generation is a major part of the local economy will face significant change over coming decades as the energy mix transitions away from being fossil fuel dependent. There is a risk that as the energy sector transitions there may be a reduction in employment opportunities for regional local communities unless alternative industries grow and flourish.

All stakeholders from local and state governments, asset owners and local community will need to work together to develop solutions for industry and jobs with strong engagement from the outset. Some of this dialogue has started and it must continue. Focus areas include training and development as well as identification of new industries and services.

Getting the social strategies right is just as important as getting the right emissions reduction policies, as the community needs to be brought on the journey over many decades as the impacts are wide ranging and effect stakeholders in many different ways.

As outlined above, opportunity for new industries exists in the form of renewable energy which will require skilled staff to operate the plants. As the pace of innovation increases, new industries will develop and the onus will be on government and business working together to develop the talent required to meet these needs.

Getting the social strategies right is just as important as getting the right emission reduction policies, as the community needs to be taken along on the journey over many decades as the impacts are wide ranging and effect stakeholders in different ways.

A (cautiously) optimistic future

Australia has historically lacked consistent government policy focused on providing long-term incentives and certainty to business needed to support the transition to a low-carbon economy and to pursue clean energy investments.

However, the outcomes at COP21 and the clean technology commitments noted above, coupled with other public-private sector drivers such as the recently launched Sustainable Development Goals¹³, indicate that the current momentum to transition Australia to a clean energy, low carbon economy is here to stay.

Organisations should re-invigorate their planning for a low carbon Australia through the following:

- Recharging current climate change and emissions policies and targets to ensure alignment with both Australian and global reduction targets and assessing whether additional transparency to key stakeholders on these matters is required
- Taking heed of the “We Mean Business” coalition commitments and understanding sector and competitor action in order to keep pace with regulatory and stakeholder expectations
- Identifying opportunities to capitalise on the support for innovation and renewable energy. New products and markets, partnerships and alliances, and economic savings and investments should all feed into business horizon scanning
- Stepping back and evaluating overall business strategy to align it with the Sustainable Development Goals. Alignment with these goals can generate mutually beneficial stakeholder relationships and thus help maintain social license to operate.

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