

Low Carbon Liquid Fuels

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Introduction

The Australian Chamber of Commerce and Industry (ACCI) appreciates the opportunity to provide comment as part of the low carbon liquid fuels industry consultation.

ACCI recognises that the transport sector must play its role by decreasing its dependence on fossil fuels if Australia is to achieve its interim emissions reduction target and realise net-zero emissions by 2050.

Transport emissions, from road, rail, coastal shipping and aviation, represent around 18 per cent of Australia's total emissions and the sector is almost entirely dependent on refined liquid fuels.¹ Road transport accounted for around 85 per cent of transport emissions or about 16 per cent of Australia's total emissions. Air transport is the next largest sector, consuming around 9 per cent of transport emissions. Rail transport produced a further 4 per cent of transport emissions and sea transport a further 3 per cent.

Australia consumed over 61.5 billion litres of petroleum-based products, including petrol, diesel and aviation fuels, in the year to March 2024.² Australia has limited capacity to refine large amounts of oil into fuel, so demand is met mainly by imports. In the year to March 2024, 86 per cent of all fuel consumed in Australia was imported (52.84 billion litres), with 68 per cent imported as refined petroleum products. All (100 per cent) of the aviation fuel consumed in Australia, around 7.45 billion litres, was imported.

Some sectors such as passenger vehicles have decarbonisation pathways through electrification. However, other sectors such as aviation, heavy freight vehicles, off-road mining and agricultural equipment, and plant and machinery will take longer to decarbonise, given the absence of affordable low-carbon engine technologies in the near term. The achievement of near-term emission reductions in these sectors will therefore likely rely on the market adoption of low carbon liquid fuels (LCLFs).

The move to LCLFs offers the opportunity to reduce dependence on imported liquid fuels by developing a sustainable low carbon liquid fuel industry in Australia. This will reduce Australia's exposure to volatility in global markets and safeguard the security and reliability of liquid fuel supply.

LCLF production and use in Australia

Biofuel production in Australia is currently very small and uses first generation processing technology. Australia has three facilities producing bioethanol from wheat starch or sugar cane, with a processing capacity of 440 million litres, and three facilities producing biodiesel from used vegetable oil (used and virgin) and tallow, with a capacity of 107 million litres.³ However, these facilities are operating well below capacity. Australia produced only 175 million litres of bioethanol in 2022, with bioethanol production steadily declining in recent years, from a peak of 317 million litres in 2017. Biodiesel production was 15 million litres in 2022, with production also decreasing in recent years from a peak of 27 million liters in 2020.⁴

¹ Climate Change Authority 2021, *Transport*. <https://www.climatechangeauthority.gov.au/sites/default/files/2021-03/2021Fact%20sheet%20-%20Transport.pdf>

² DCCEE 2024, *Australian Petroleum Statistics*, <https://www.energy.gov.au/publications/australian-petroleum-statistics-2024>.

³ Ethanol Producer Magazine 2023, *Biofuel Consumption In Australia Remains Minimal in 2022*. <https://ethanolproducer.com/articles/report-biofuel-consumption-in-australia-remains-minimal-in-2022-19909>

⁴ Department of Agriculture, Fisheries and Forestry 2022, *Snapshot of world biofuels*, December 2022. <https://www.agriculture.gov.au/sites/default/files/documents/december-2022-snapshot-of-global-biofuel-market.pdf>

The most common use of biofuels is the mixing of bioethanol with petroleum at a rate of 10 per cent to produce E10. Blending of bioethanol at rates of 15 to 20 per cent is possible, but blending at higher rates than this would require engine modification. There are also small volumes of E85 (85 per cent ethanol) produced and used in heavy vehicles.

Biodiesel is also most commonly blended with diesel at proportions of 5 to 20 per cent (R5, R10 and R20).

A small number of renewable diesel projects have been announced in recent years, but these refineries are still seeking finance and construction is yet to begin. While renewable diesel is not currently produced at a commercial scale in Australia, there are examples of renewable diesel being used in a small number of demonstration models of heavy vehicles. Second generation renewable diesel has better compatibility with existing infrastructure and current internal combustion engine technology. It does not require engine modifications to be used without blending.

To date, there is no Sustainable Aviation Fuel (SAF) production in Australia. Small volumes of SAF are currently used in Australia's aviation sector on international flights from countries with sustainable fuels requirements. SAF is broadly compatible with existing refueling infrastructure and can be used in engines without blending.⁵ However, due to the small volumes produced relative to demand, it is typically blended with jet fuel at rates of 10 per cent.

Australia's LCLF opportunity

The CSIRO SAF Roadmap show a range of pathways to producing SAF, as well as renewable diesel, through biogenic processes using crop residues, municipal wastes and oil-seeds as feedstocks.

Australia benefits from access to large volumes of agricultural and forestry residues, as well as municipal waste, that can be used as feedstock for LCLF production through biogenic processes. Through fermentation processes these can be used to produce renewable diesel and SAF.

Australia is also a large producer and exporter of oil-seeds, including canola, sunflower, cotton-seed and other oils. While some of this is used for domestic food consumption, the bulk of it is exported. The majority of Australia's \$5.76 billion in canola exports in 2021-22 were used to make biofuel in the European Union.⁶ This would suggest there is significant potential to develop renewable diesel and SAF production based on canola that is currently exported, under the right policy setting and incentive.

Other pathways, such as power-to-liquid, using green hydrogen and CO₂ are possible, but at the current stage of technology development it is considerably more expensive to produce and is not cost competitive with biogenic processes.

The CSIRO Sustainable Aviation Fuel Roadmap identified Australia could be well placed to become a globally significant producer of SAF and other renewable fuels. With significant volumes of oil-seeds, crop residues and municipal waste, there is sufficient feedstock to supply almost 5 billion litres of SAF production in Australia, or around 50 per cent of forecast jet fuel demand in 2025.⁷ The transition to SAF in the aviation sector presents a significant opportunity for Australia.

⁵ CSIRO 2023 *Sustainable Aviation Fuel Roadmap*. <https://www.csiro.au/en/research/technology-space/energy/sustainable-aviation-fuel>

⁶ Department of Agriculture, Fisheries and Forestry 2022, *Snapshot of world biofuels*, December 2022. <https://www.agriculture.gov.au/sites/default/files/documents/december-2022-snapshot-of-global-biofuel-market.pdf>

⁷ SAF and renewable diesel are complementary products. It is unlikely all feedstock and production will be dedicated to SAF.

Australia's Bioenergy Roadmap sets an objective to grow Australia's production to meet 10 per cent of liquid fuel demand (around 6 billion litres) by 2030.⁸ This includes both renewable diesel and SAF, with the optimum mix of the LCLF types to be determined by the market. To achieve this 12-fold increase in LCLF production capacity within the next six years would require considerable investment in new facilities.

Due to the dispersed nature of the feedstocks for LCLF production, being low value crop residues or municipal wastes, it is uneconomic to be transporting these inputs long distances (hundreds of kilometres) to support large-scale production facilities. Therefore, a large number of smaller production facilities will need to be developed, scattered throughout regional Australia close to the feedstock source.

'Green premium'

The demand for LCLFs is highly dependent on its cost competitiveness relative to fossil fuel alternatives.

Energy prices are highly volatile and the Australian economy is very sensitive to movements in energy prices. The heavy reliance on imports of liquid fuels makes Australia very vulnerable to global events, as the COVID crisis and the war in the Ukraine have shown. Sharp increases in liquid fuel prices can weigh heavily on economic activity and contribute greatly to inflationary pressures.

The International Energy Agency (IEA) tracking of biofuels identifies that the average production costs of low-carbon biofuels derived from non-food feedstock, such as wastes, crop residues and dedicated non-food crops, is double to triple that of their fossil fuel equivalents.⁹ The consultation paper indicates that some third and fourth generation products, such as SAF produced using Power-to-Liquid process (combining hydrogen and CO₂), can be up to five times more expensive. While the costs are expected to decrease as technology improves and LCLFs are produced at scale, it will be some time before LCLFs are cost competitive with their fossil fuel alternatives. The IEA expects that these costs could decline as much as 27 per cent over the next decade, but there will still be a substantial gap, or 'green premium', in the price of LCLFs relative to their fossil fuel equivalents.

Australian consumers and businesses have shown some willingness to preference sustainably sourced products over a less environmentally friendly product. If sustainably sourced liquid fuels can be produced at prices that are cost competitive with the equivalent fossil fuel product, and have the same production performance, consumers and businesses will favour the sustainably sourced product.

However, consumers and businesses are rarely prepared to pay a 'green premium' for a sustainably sourced product. While attitudes are shifting for some products, with a small proportion of customers willing to pay a premium for sustainably sourced products as part of achieving their Environmental, Social and Governance (ESG) objectives, this price differential may not be sufficient to overcome the higher production cost differential of sustainable products.

Further, the Safeguard Mechanism Reforms is creating latent demand for LCLFs, as large emitters using liquid fuels, such as road freight operators, airlines and manufacturers, are required to progressively reduce their emissions. However, with the 'green premium' of LCLFs, this is raising production and delivery costs, affecting the international competitiveness of some industries.

⁸ enea Consulting and Deloitte 2021, *Australia's Bioenergy Roadmap*. ARENA. <https://arena.gov.au/assets/2021/11/australia-bioenergy-roadmap-report.pdf>

⁹ IEA 2024, <https://www.iea.org/energy-system/low-emission-fuels/biofuels#tracking>

Recommendation:

- With the cost of LCLF between two and five times more expensive (dependent on the technology) and Australian consumers and businesses rarely willing to pay a 'green' premium for sustainably sources products, support and incentive measures are needed to stimulate investment and reduce the cost differential of LCLFs relative to their fossil fuel alternatives.

Mandates

NSW and Queensland have mandates for the sale of ethanol blended fuels, with all fuel retailers required to have petrol-ethanol blends available, with ethanol at least 4 per cent (Queensland) to 6 per cent (NSW) of all petrol sold (i.e. E10 representing 4 to 6 litres per 10 litres of total petrol sold).¹⁰ NSW and Queensland also have mandates on biodiesel, requiring biodiesel to make up 0.5 per cent (Queensland) to 2 per cent (NSW) of all diesel sold. To meet these requirements, E10 petrol and R5/R10 diesel blended fuels are typically sold at a discount relative to the lowest cost alternative (ULP91 and diesel). The cost of these measures, which were designed to promote the products of biofuels producers, are mainly shouldered by the retailer, giving rise to significant issues of inequity

These mandates have been in place for many years (in NSW since 2007 and in Queensland since 2017). Despite being heavily discounted by retailers, E10 petrol and R5/R10 diesel are not preferred by customers. Retailers typically struggle to meet the 4 to 6 per cent ethanol sales or 0.5 to 2 per cent biodiesel requirements, with neither state achieving their target rate of ethanol or biodiesel substitution.

In NSW, 17 years of operation has resulted in the level of ethanol substitution in petrol being just 2.8% compared with the longstanding target of 6%. In Queensland, the 7 years of operation of the mandate has resulted in 3.1% substitution relative to a target of 4%.

The NSW and Queensland governments have subsequently elected to soften these mandates by adopting a principle of 'best endeavours' on fuel wholesalers and fuel retailers. Retailers are required to stock these first generation biofuels and market them in a high profile manner – effectively doing all they reasonably could to encourage fuel purchases.

Given the experience with mandates in NSW and Queensland, alternative measures that do not distort market prices and place an excessive burden at the retail end of the supply chain should be considered to generate demand for LCLFs.

Recommendation:

- Mandates on the sale of blended ethanol and biodiesel should be removed as they distort the price and lead to inequity in the supply chain, but have proven ineffective in generating demand.

¹⁰ Fair Trading NSW 2022, Minimum biofuel requirements. <https://www.fairtrading.nsw.gov.au/trades-and-businesses/business-essentials/service-stations>; Queensland Government 2018, Queensland biofuels mandates. <https://www.business.qld.gov.au/industries/manufacturing-retail/retail-wholesale/selling-fuel-qld/qld-biofuels-mandates>

Investment

The higher cost of LCLFs relative to fossil fuels is the biggest barrier to the use of biofuels in Australia. Without government policy and support measures to attract investment in production and drive demand, LCLFs are unlikely to gain more than a very minor share of the market.

With little existing infrastructure, new production facilities will need to be developed to establish a LCLF industry in Australia. In developing new facilities, Australia will need to compete in international markets for investment dollars. Attracting the necessary investment for these production facilities may prove challenging without regulatory reform and the right policy settings to support this investment.

Australia is a high-cost producer, due to high labour and material costs. Stringent environmental standards also make development approval processes arduous and can result in very long investment lead times for major projects. To support the development of new LCLF production facilities, regulatory reforms are needed to remove barriers and fast-track environmental approval processes.

In the development of a LCLF production sector, Australia is likely to face strong competition from less developed countries in our region, with access to similar large volumes of agricultural and forestry feedstocks, but much lower labour and construction costs and lower environmental standards. Biofuel production is already growing strongly in our region, particularly Indonesia, Malaysia and India, thanks to strong domestic policies, growing domestic demand and export-driven production.¹¹ Over the next five years, Asian countries are expected experience the largest growth in demand. Blending targets for biodiesel in Indonesia and Malaysia and India's ethanol policies will drive most of this growth.

Australia is also likely to face strong competition for investment in low carbon liquid fuel production from the United States and European Union. These countries offer substantial the production subsidies and other support through the Inflation Reduction Act (IRA – US) and the Green Deal Industrial Plan (Europe). These countries are also further advanced in the development of biofuels industries than Australia.

Recommendation:

- To support investment in new production facilities, regulatory reforms are needed to remove barriers and fast-track environmental approval processes.
- Australia competes in a global market, so investment support must be targeted at LCLF products where Australia has a competitive advantage.

The expected rate of support required

According to the Australian Institute of Petroleum, in the week of 7 July 2024 wholesale international fuel prices ranged from 92.9 cents per litre for Singapore petrol (MOGAS95) to 96.8 cents per litre for Singapore diesel (Gasoil 10ppm).¹² At the pump, average retail prices were 186.0 cents per litre for unleaded petrol (ULP91), 201.1 cents per litre for premium unleaded (PULP95), 183.2 cents per litre of

¹¹ Department of Agriculture, Fisheries and Forestry 2022, *Snapshot - World biofuels trade*. <https://www.agriculture.gov.au/about/news/snapshot-world-biofuels-dec-22>

¹² Australian Institute of Petroleum 2024, *Weekly Prices Report*. Accessed 8 July 2024. www.aip.com.au/pricing/weekly-prices-reports

E10 and 194.5 cents per litre for diesel. The difference between the wholesale and the retail price includes fuel excise (charged at a rate of 49.6 cents per litre), as well as freight and retail costs.

The wholesale premium for ethanol and biodiesel (at current exchange rates) is between \$1.20 and \$1.40 per litre relative to fossil fuels. Therefore, an expected rate of support for a competitive production incentive scheme would need to be in excess of \$1.20 per litre.

Similarly, the average jet fuel price in the Asia and Oceania region was 240.75 US cents per gallon (equivalent to 94.3 AU cents per litre¹³). With production costs of SAF also more than double that of their fossil fuel equivalents, the level of support under a production tax incentive or contract for difference scheme would also need to provide an incentive in excess of \$1.20 per litre.

Recommendation:

- With the production cost of LCLFs currently in excess of double that of fossil fuels, the rate of support required would need to be in excess of \$1.20 cents per litre.

Options to support domestic LCLF production

A mix of different options will be needed to attract the private investment necessary to increase domestic production of LCLFs. Production incentives are necessary to overcome the high cost differential of LCLFs, which are currently between two and three times that of fossil fuel equivalents. Investment incentives and support will also be necessary to assist in financing new production facilities.

Production incentives offer a relatively effective form of government support for emerging industries, where incumbent industries (such as fossil fuels) benefit from externalities (generating carbon emissions). Producers only access the incentive after the production facility is established and once production begins, with the incentive provided on a per unit of production basis.

The production tax incentive is typically a time limited incentive involving a tax credit per unit of production. This gives the investor a level of certainty of a reasonable return on investment in the initial years of production, by offsetting some of the difference between the cost of production and the lower market price of the product. Unlike other options, delivery of the incentive through the tax system provides an efficient means of delivery, avoiding high administrative burden and potential project selection distortion.

Similarly, contracts-for-difference (CfDs) also provide businesses with certainty of the price they will receive for their products. A CfD involves an auction process where producers bid to produce a set volume at a specified price, with the government covering the difference between the bid price and the market price at the time of sale. Where the bid price is higher than the market price, the producers would be required to pay back the difference to the government. The payment under a CfD scheme is likely to decrease over time as more producers enter the market and the cost of production reduces with increased competition, as well as new technology and innovation.

CfDs are a proven approach to incentivising investment in renewable energy, with state governments implementing contracts for difference schemes and auctions for different aspects of the renewable energy buildout. For example, the ACT Government has initiated CfDs for wind power generation, Queensland for solar PV, South Australia for battery storage and more recently Victoria for wind and solar.

¹³ Based on the exchange rate on 8 July of AU\$1.00=US\$0.6744 (RBA) and 3.785 litres per gallon.

However, CfDs have their drawbacks, including higher administrative burden associated with the tendering processes and contract management. It also risks inefficiency and market distortion if not managed with rigorous governance procedures. Therefore, a time-limited production tax incentive is likely to be a more efficient approach to offsetting the higher production costs, due to it being delivered through the tax system.

In addition to a production incentive, consideration should also be given to the removal of fuel excise from the LCLF products and/or the LCLF component of blended fuels. The excise rate on petrol and diesel is currently 49.6 cents per litre, with blended fuels subject to fuel excise at the same rate as fossil fuels. To encourage the use of LCLF and blended fuels, consideration should be given to lowering the excise on blended fuels. With the cost differential for ethanol and renewable diesel over \$1.00 per litre, fuels blended at 10 per cent (E10 and R10) require a subsidy of greater than 10 cents per litre to be cost competitive with fossil fuels. This could readily be provided through a reduction in fuel excise for blend fuels.

Similarly, aviation fuels (gasoline and kerosene) have a fuel excise of 3.56 cents per litre. The removal of fuel excise from SAF blended aviation fuels, will also reduce the cost and support greater use of SAFs.

While production incentives provide some certainty to the producer by assisting in covering some of the higher costs of LCLF production, it is unlikely to be successful as a standalone measure.

These will need to be complemented with other support measures, such as low interest loans or capital grants, to address the high cost of investment to construct a production facility. There are already a number of incentive available for investment in renewable energy through the Clean Energy Finance Council (CEFC), Australian Renewable Energy Agency (ARENA), National Reconstruction Fund (NRF), Northern Australia Infrastructure Fund (NAIF). Access to these funds should be extended to investment in low emissions processing technology for LCLFs.

Further, while production incentives and investment support are necessary to develop the supply side, it is also necessary to create a market for LCLFs by stimulating demand. Australian governments should lead by example in the adoption of new technologies and to assist in the creation of a market for LCLF. Federal, state and local governments operate very large fleets of vehicles and are currently very large consumers of fossil fuel. Government procurement contracts offer a significant opportunity to create demand for LCLFs and assist the industry to establish. Similarly, the Australian Defence Force operates a large fleet of aircraft, ships and heavy vehicles that would support the early development of SAF and biodiesel in Australia.

Recommendation:

- A combination of policy measures will be needed to drive private investment in LCLF, including both investment incentives and production incentives.
- Production tax incentives are an efficient approach to offsetting the higher production costs, as they can be time limited and delivered through the tax system.
- Remove fuel excise from the LCLF products and/or the LCLF component of blended fuels
- Access to existing funds supporting investment in renewable energy infrastructure should be extended to investment in LCLF, including CEFC, ARENA, NRF and NAIF.
- Australian government departments and agencies (Federal [including Defence], state and local) should lead by example through use of LCLF in their vehicles. Government procurement contract will create a stable base level of demand that will support the development of a domestic market for LCLF.

The design of support mechanisms

As a general rule, Australia should not provide incentives to establish and sustain industries that cannot be internationally competitive over the long term. It is essential that any biofuel industry developed in Australia is sustainable over the longer term without government support.

Any program to support the development of the emerging LCLF industries must be time limited, with an expectation that after a period of time production will be sustainable. Support should only be provided for emerging industries in the establishment phase, to enable the technologies to be refined and production to be scaled up and commercialised, so it can achieve the economies of scale necessary to be profitable over the longer term.

The proposed 10-year time frame for a production tax incentive should be sufficient for a competitive market for LCLF to develop and to enable production facilities to scale-up and become competitive.

Recommendation:

- Any government support for LCLFs must be time limited, to support emerging industries in the establishment phase.
- Government support should not be provided to establish industries that cannot be internationally competitive and sustainable over the long term.

Production shares and thresholds

SAF and renewable diesel are complementary products and there is a trade-off in the proportion of each of fuel-types produced at a facility. Australia should not be looking to rely on domestic production to meet all domestic demand for all LCLF types. Nor is it appropriate to set production shares and thresholds for the production of SAF and biodiesel. This is likely to be counterproductive and lead to inefficient outcomes.

Australia operates in an open global market. There are a number of factors that will determine the competitiveness of Australia LCLF products in international markets. Australian investment in LCLFs will be drawn to products where we are most competitive.

While government incentives are necessary to attract investment and assist the industry to establish, it is important to let the market decide where, when and how to invest and to produce. Where Australia does have an international competitive advantage in the production of one LCLF, then it should focus on the production of that fuel type. In fuel types where Australia is less competitive, it should import that product.

Recommendation:

- Government support should not be prescriptive on the LCLF type and where it is produced.
- It is important to let the market decide where, when and how to invest and to produce.

Emissions and sustainability criteria

To be credible, the eligibility criteria for producers to receive support under a production incentive scheme must include a threshold for emissions reduction below conventional fossil fuels.

A clear definition of what constitutes a low carbon liquid fuel is a necessary starting point. It is also important to have different thresholds for the different fuel types, recognizing the range of inputs in production, processes and level of refinement for the various LCLF types. These thresholds need to be consistent with international benchmarks as it is likely Australia will be an importer of some fuel types and an exporter of others.

The level of the threshold should be set relative to the technology used to produce the fuels, as some fuels require less processing, so can be produced at lower emissions than others. For example, the production of biodiesel from oilseeds involves little processing, with emissions related mainly to the sowing, harvesting, pressing and transport of the oil-seeds. As this requires little processing, the emissions involved in production are likely to be lower than the production of SAF, which requires a higher level of processing and refining, so a higher threshold may be more appropriate for SAF.

The Safeguard Mechanism requires that any new production facility be established using best practice, with emissions at the lowest 10 per cent the type of production being undertaken.

Given this starting point, with a new LCLF production facility already operating at international best practice, and the rate of technology development to achieve further emissions reduction, it is unlikely that a new LCLF production facility will be able to achieve significant emissions reductions in the near to medium term. Therefore, a scaling approach to lower emissions thresholds for LCLFs over time is likely to be counterproductive in attracting investment into biofuel production.

Setting threshold based on current best-practice production techniques and providing producers access to carbon credit units for production below these thresholds is more likely to stimulate the greatest investment in LCLFs and incentivize innovation to drive further emissions reduction in biofuel production.

Recommendation:

- A clear definition of what constitutes a low carbon liquid fuel is necessary
- Different emissions levels should be applied to the different fuel types, dependent on the technology used and level processing/refinement needed.
- Due to the Safeguard Mechanism requirements, any new production facility will be established using international best practice, so further constraints requiring emissions reduction overtime will be counterproductive to attracting investment.

Certification of LCLFs

ACCI agrees that the production of LCLF should be included in the Guarantee of Origin scheme to allow tracking of emissions associated with the production and use of the LCLFs.

It is also important that any certification arrangements, particularly for those that are internationally traded such as aviation fuels, should align with international schemes, such as the CORSIA scheme developed by the International Civil Aviation Organisation.

Recommendation:

- LCLF production should be included in the Guarantee of Origin scheme.
- The Guarantee of Origin scheme should align with international schemes as Australia will be trading LCLFs in international markets

About ACCI

The Australian Chamber of Commerce and Industry represents hundreds of thousands of businesses in every state and territory and across all industries. Ranging from small and medium enterprises to the largest companies, our network employs millions of people.

ACCI strives to make Australia the best place in the world to do business – so that Australians have the jobs, living standards and opportunities to which they aspire.

We seek to create an environment in which businesspeople, employees and independent contractors can achieve their potential as part of a dynamic private sector. We encourage entrepreneurship and innovation to achieve prosperity, economic growth, and jobs.

We focus on issues that impact on business, including economics, trade, workplace relations, work health and safety, and employment, education, and training.

We advocate for Australian business in public debate and to policy decision-makers, including ministers, shadow ministers, other members of parliament, ministerial policy advisors, public servants, regulators and other national agencies. We represent Australian business in international forums.

We represent the broad interests of the private sector rather than individual clients or a narrow sectional interest.



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