Australian Government

Corporations Amendment (Emissions Reduction Fund Participants) Regulation 2015

Consultation Paper
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CONSULTATION PROCESS

REQUEST FOR FEEDBACK AND COMMENTS

All information (including name and address details) contained in formal submissions will be made available to the public on the Australian Treasury website, unless it is indicated that you would like all or part of your submission to remain confidential. Automatically generated confidentiality statements in emails do not suffice for this purpose. Respondents who would like part of their submission to remain confidential should provide this information marked in a separate document.

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CLOSING DATE FOR SUBMISSIONS: 13 FEBRUARY 2015

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1. SUMMARY

This discussion paper outlines the Government's proposed exemptions from the *Corporations Act 2001* and *Corporations Regulations 2001* (the corporations law) for participants in the Emissions Reduction Fund's (ERF) processes. These exemptions are contained in the draft *Corporations Amendment (Emissions Reduction Fund Participants) Regulation 2015*.

The exemptions reflect the Government's commitment to simplify the application of the financial services provisions of the corporations law for ERF participants. The generic financial services laws are not well suited for protecting participants against the risks associated with ERF processes and, in some cases, impede the efficient and effective operation of the ERF. In response, the Government is developing alternative protections specifically targeted at regulating activities relating to the ERF.

Under the proposed exemptions, most project proponents, aggregators and carbon service providers would not be required to hold an Australian Financial Services Licence (AFSL) or provide Product Disclosure Statements (PDSs) so long as they do not provide financial services, as defined under the corporations law.

This paper outlines the justification for and the technical operation of the proposed exemptions. This discussion paper also provides some worked examples showing who might and might not be required to hold an AFSL.

The Government is seeking views on whether these proposed exemptions are appropriate and whether further exemptions are required.

2. BACKGROUND ON THE EMISSIONS REDUCTION FUND (ERF)

The ERF is the centrepiece of the Government's Direct Action Plan to reduce Australia's carbon emissions. It is operated by the Clean Energy Regulator (CER). The CER, through the ERF, will purchase emissions reductions identified as the lowest cost through a reverse auction process. The ERF was established by the *Carbon Farming Initiative Amendment Act 2014* which commenced on 13 December 2014. Participation in the Emissions Reduction Fund will be open to individuals, sole traders, companies, local, state and territory government bodies and trusts.

ERF participants will need to apply to the Clean Energy Regulator to register a project under an approved methodology. Participants can only register projects if they have the responsibility and legal right to carry out those projects.

Persons, known as project proponents, may make bids in an ERF reverse auction. Once a project is registered, project proponents can enter into contract with the Government for future delivery of an accepted volume of ACCUs at a price determined in the reverse auction process. This is known as a carbon abatement contract. Only registered projects will be considered in the contract establishment and auction process. The contract establishment process involves due diligence checks to confirm that the project is credible and can deliver the stated emissions reductions within the timeframes indicated.

Project proponents will need to submit regular reports on their registered projects, including reporting on their emissions reductions. Project proponents who have a contract with the Clean Energy Regulator will deliver ACCUs according to the schedule in their contract, and will then be paid at the price bid at auction and set out in the contract.

Carbon service providers may assist project proponents, including aggregators, in verifying their emissions, making a bid in an ERF auction, and other administrative functions.

Secondary markets may develop over time for buying and selling ACCUs. If a proponent has excess ACCUs, it may sell them to other parties, such as other project proponents or entities voluntarily reducing their emissions footprints. If a proponent has insufficient ACCUs, it may purchase ACCUs from other parties to meet its contractual obligations.

2.1 THE AGGREGATION PROCESS

Aggregation occurs when discrete or separate emissions reductions activities are combined into one project and/or bid.

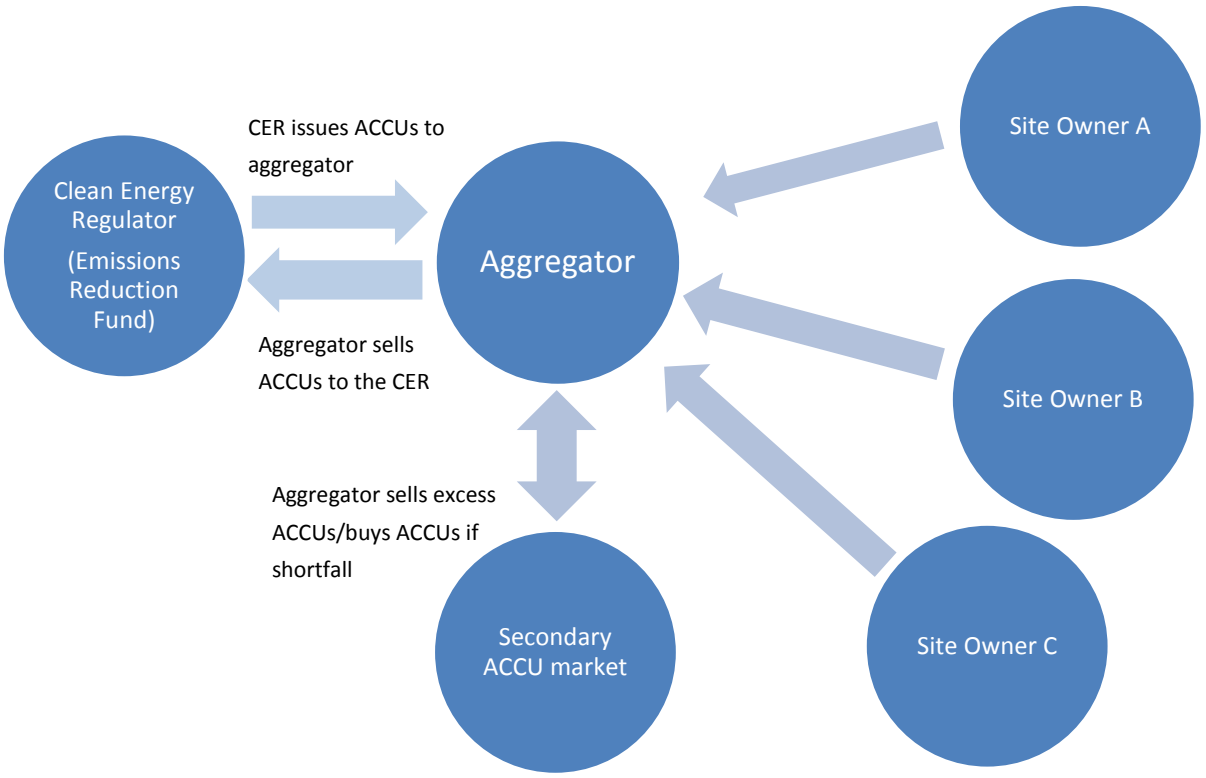
There are two broad categories of aggregation:

- The first is project aggregation, when emissions reduction activities which are covered by a single approved methodology are grouped together and registered as a single project. The activities could be carried out on multiple sites.
  - For example, an aggregated project under the commercial building methodology might consist of energy efficiency activities in several buildings in one or more states and territories.
- The second is contract aggregation, when multiple projects are grouped into a single bid for the purpose of receiving a single carbon abatement contract through an ERF auction. In this case, the projects could be covered by different approved methodologies.
  - For example, a project proponent who has registered a commercial building project, a landfill gas project and a savanna fire management project could bundle these projects into a single bid for an ERF auction and contract.

In this paper, the proponent of such projects will be referred to as the 'aggregator', and the owners of the sites will be referred to as 'site owners.'

Diagram 1 below sets out an example of a possible aggregation model.

Diagram 1: A possible aggregation model



Example: An organisation acts as an aggregator by aggregating emissions reductions from farmers (site owners) who plant trees. The aggregator registers the projects and qualifies to participate in the auction with the CER. The aggregator then participates in the auction as a bidder and enters into a carbon abatement contract with the CER. Subject to reporting and delivery of contracted emissions reductions, the aggregator is issued with ACCUs. If it generates more ACCUs than necessary to meet its obligations to the ERF, it can sell them on the secondary market.

3. Overview of proposed exemptions

Under the current law, carbon abatement contracts and aggregation arrangements may be regulated as financial products, and some advice provided by carbon service providers may be regulated as a financial service under the financial services provisions in the corporations law (the financial services regime).

If exemptions are not provided, most project proponents, aggregators, and carbon service providers would be required to hold AFSLs and to meet the conduct and disclosure obligations contained in the financial services regime. This increases the regulatory burden on ERF participants – a burden which would only be justified if it improved regulatory outcomes in a manner that could not be achieved by less regulatory alternatives.

Applying the generic financial services provisions to ERF processes may result in unintended regulatory outcomes without protecting participants against certain risks. For example, aggregation arrangements which adopt sensible risk management mechanisms would face higher regulatory burdens, discouraging aggregators from adopting these mechanisms and therefore increasing the risk exposure to members of that arrangement.

Therefore, the proposed exemptions will provide that:

- carbon abatement contracts, which a proponent and CER enter into after a successful ERF bid, would not be regulated as financial products;
- certain eligible aggregation arrangements would not be regulated as financial products;
- carbon service providers who only provide financial product advice which is incidental to technical advice relating to an ERF project would not be regulated as financial advisers.

The Government is developing alternative regulatory protections to protect against risks associated with ERF processes. The Government is developing a standardised disclosure document that will highlight the risks and benefits associated with participating in an aggregated project. It is also developing best practice aggregation contracts which will include standard terms protecting the parties to the contract.

The financial services regime will continue to apply to financial services that do not fall within the scope of the proposed exemptions to protect against the risks associated with these services. Thus, financial services in relation to ACCUs which pose similar risks to other financial services, such as the brokering of trades, will continue to be regulated in a similar manner.

The Government is seeking views on whether further exemptions are appropriate. Two potential exemptions the Government could grant would provide that:

- an aggregator is not considered to be dealing in ACCUs on behalf of a site owner if ACCUs were issued to the aggregator by the CER as a result of carbon abatement provided by that site owner; and
- an aggregator is not considered to be providing custodial and depository services to a site owner because it holds ACCUs which were issued by the CER as a result of carbon abatement provided by that site owner.

The following discussion outlines proposed exemptions in further detail, including through worked examples illustrating when an AFSL may or may not be required.

DISCUSSION QUESTION

Question 1 Are any further amendments to the corporations law required for the efficient operation of the ERF?

4. FINANCIAL PRODUCTS

The corporations law applies to financial services provided in relation to financial products, including derivatives, managed investment schemes and ACCUs. Generally, a person who carries on a business of providing financial services must hold an AFSL. Conduct and disclosure obligations also apply.

4.1 Derivatives

4.1.1 What is a derivative?

A derivative is a complex form of financial product whose value is determined by the value of an underlying asset. For example, a forward contract for the future delivery of ACCUs is a derivative as its value is determined by the value of the underlying ACCUs.

4.1.2 Carbon abatement contracts may be derivatives

A carbon abatement contract is the contract a project proponent enters with the CER after it successfully bids at an ERF auction. This may be considered a derivative as the value of the contract depends on the value of ACCUs which may vary for equivalent future sale and purchase agreements.

The regulatory treatment of derivatives that are not traded on financial markets differs from other financial products. All parties to a derivatives contract are considered to be issuers of that product – whereas, in substance, the issuer of a carbon abatement contract is the Clean Energy Regulator. As a consequence of being treated as an issuer of a derivative (instead of being a purchaser), the project proponent is required to hold an AFSL even if it only deals in the derivative on its own behalf. A purchaser would only be required to hold an AFSL if it was purchasing financial products on behalf of another person, such as a site owner.

Entities using derivatives for hedging purposes are presently exempted from financial licencing requirements, but project proponents are unlikely to benefit from this exemption. A person dealing in derivatives does not currently need an AFSL if that dealing is to manage a financial risk arising in the ordinary course of a business and the dealing is not a significant part of a person's business. However, since entering carbon abatement contracts is likely to be a significant part of most proponents' businesses, most proponents would need to hold an AFSL.

4.1.3 Proposed exemption for carbon abatement contracts

Ordinarily, a derivatives trader is required to be licenced to provide some protection to the other party to the derivatives contract. As the other party of a carbon abatement contract is the Clean Energy Regulator, which does not require such protection, the requirement that parties entering a carbon abatement contract hold an AFSL represents an unnecessary regulatory burden. Therefore, this paper is proposing to exclude all carbon abatement contracts from the definitions of 'derivative' and 'financial product' in the Corporations Act.

4.1.4 Aggregation arrangements may also be derivatives

Aggregation arrangements may also be considered derivatives in some circumstances, for example, if the aggregation contract required payments linked to the price of an ACCU in a carbon abatement contract. Most aggregation contracts are not likely to be derivatives because they fall within the existing exemptions for contracts for provision of future services or, in some cases, for delivery of physical goods.

However, it is uncertain whether all likely aggregation models would benefit from these exemptions. This could introduce competitive neutrality issues if some models become regulated and some are not regulated.

4.1.5 Proposed exemption for eligible aggregation arrangements

To provide regulatory certainty in respect of aggregation arrangements already benefitting from the proposed exemption from the definition of 'managed investment scheme', it is proposed that eligible aggregation arrangements also be exempted from the definition of 'derivative' in the Corporations Act.

Example 1: Project proponent

A project proponent makes a successful bid in an ERF auction. It enters into a carbon abatement contract with the CER to deliver 1,000 ACCUs each year for seven years. Without the exemption, there is a risk this contract would be considered a derivative. If so, the proponent would be required to hold an AFSL as it would be considered to be issuing that derivative to the CER. However, the exemption is clear – a carbon abatement contract is not a derivative or a financial product – and the proponent would not be required to hold an AFSL for that reason.

DISCUSSION QUESTIONS

Question 2 Is the proposed exemption appropriately drafted?

Question 3 Are further exemptions from the regulation of derivatives required?

4.2 Interests in a Managed Investment Scheme (MIS)

4.2.1 What is a MIS?

A MIS is a kind of legal vehicle used for collective investment. The *Corporations Act 2001* (the Act) defines it as a scheme in which:

- people (members) contribute money to acquire rights to benefits produced by the scheme;
- the contributions are pooled, or used in a common enterprise, to produce financial benefits, or benefits consisting of rights or interests in property, for the members; and
- the members do not have day-to-day control over the operation of the scheme.

Interests in a MIS are a kind of financial product and are regulated under Chapter 7 of the Act. Registered MIS, which are schemes marketed to retail clients, are also regulated under Chapter 5C of the Act.[1]

1 A MIS is required to be registered generally if there are any retail members and there are at least 20 members or the scheme is promoted by a person in the business of promoting MIS or an associate of such a person.

The responsible entity (RE) of a registered MIS, which operates the scheme, must be a public company, hold an AFSL and comply with various statutory duties. One of the requirements of holding an AFSL is that the RE must have adequate financial resources to act as an RE. ASIC Regulatory Guide 166 describes the net tangible asset requirements that an RE must meet under ASIC Class Orders. For a registered MIS where the scheme assets are held in custody, the RE must generally hold the greater of:

- $150,000;
- 0.5 per cent of the average value of the scheme property; or
- 10 per cent of average responsible entity revenue.

Other requirements under Chapter 5C include the requirement that the MIS have a constitution and compliance plan in accordance with the Act.

4.2.2 Aggregation arrangements may be MIS

An aggregation arrangement under the ERF may be a MIS, depending on how the arrangement is structured. This is because site owners may be considered to be contributing and pooling their services (or goods) to obtain proceeds from selling the ACCUs generated.

Some mechanisms that improve the sharing of risk and reward between the aggregator and site owners make the aggregation arrangement more likely to be considered a MIS. Such arrangements are more likely to be commercially acceptable to both aggregators and site owners, but the regulatory consequences of being regulated as a MIS could deter the adoption of such risk management mechanisms.

An arrangement is also more likely to be found to be a MIS where there are arrangements to deal with over- and under-issuances of carbon abatement internally within the arrangement. For example, an aggregation contract may include a clause covering the use of excess ACCUs generated by an over-performing site owner to make up for a shortfall resulting from an under-performing site owner. Such arrangements would minimise risk of under-production for individual site owners and so minimise under-production risk across a portfolio of projects for the aggregator.

Without amendment, the aggregator would have to become the responsible entity of a registered MIS. It would be subject to financial resource requirements in the form of net tangible asset requirements. These may be onerous for smaller schemes. For example, an aggregator that delivers 2000 tonnes of emissions reductions per annum at an assumed price of $10/tonne would have annual revenue of only $20,000 per annum yet it would need to hold at least $150,000 in net tangible assets for the duration of the arrangement.

4.2.3 Proposed exemption for aggregation arrangements

Aggregation arrangements are dissimilar from other MIS in a number of ways so the regulatory treatment of a MIS may be inappropriate for many aggregation arrangements and can act as a key regulatory barrier to aggregation.

Aggregation arrangements are primarily for the purpose of generating carbon abatement, rather than for the primary purpose of collective investment. Aggregation arrangements are less complex than other MISs and pose different risks. They are essentially single purpose arrangements solely for the generation and sale of ACCUs that do not require, for example, the analysis and allocation and

re-allocation of members' funds to shares of many different companies. The main asset of the aggregation arrangement is likely to be principally a single ERF contract with some residual dealings in ACCUs.

The generic financial services law does not adequately protect members of an aggregation against risks associated with aggregation, such as changes in the price for ACCUs, and disincentivises the use of risk mitigation mechanisms. As such, the financial services regime could actually increase the risk exposure of site owners.

The draft regulation therefore provides a targeted exemption for aggregation arrangements from the definition of 'managed investment scheme'. The exemption is not intended to extend to schemes investing in or funding emissions offsets projects. Genuine investment schemes will continue to be regulated as MIS. Therefore, a scheme in which members contribute money or ACCUs to the scheme would not be exempt.

The proposed exemption does not need to exempt all possible aggregation arrangements. Instead, it is intended to provide a safe harbour that allows aggregation to be undertaken in an efficient and risk-effective manner.

Example 2: A forestry aggregation arrangement

Hans, who is an aggregator, contracts with thirty farmers to create an aggregation arrangement with the intention that Hans would bid as the project proponent into the ERF. The farmers will plant trees on their land, generating carbon abatement equivalent to 100 ACCUs each. One farmer, Zoe, is concerned that she may produce less abatement than expected. To manage this risk, the aggregation contract states that if one farmer produces more abatement than expected and another farmer produces less than expected, then the excess abatement will be deemed to make up the shortfall of the second farmer.

Although this clause is a sensible risk management tool, it would have made this aggregation arrangement a managed investment scheme if not for the proposed exemption. Hans' business would be required to hold an AFSL, it would have to become the responsible entity of the registered scheme and meet the financial requirements applicable to responsible entities. These requirements may have made the arrangement financially unviable. Hans may decide not to adopt such a clause even though it improves the operation of his aggregation arrangement.

The proposed exemption would exempt this aggregation arrangement from the definition of 'managed investment scheme' and 'financial product'. The farmers undertake the carbon abatement by planting trees. If, in an alternate scenario, the farmers had permitted Hans to enter their land to plant trees then they would be providing one of the means (i.e. the land) of undertaking abatement to him. This would also be exempt.

Under the proposed exemption, Hans' business would not be required to hold an AFSL or comply with the conduct and disclosure requirements of the financial services regime.

Example 3: An aggregation/investment scheme

Another aggregator, James, contracts with several farmers to create an aggregation arrangement with the intention that they would bid into the ERF. The contract contains the same clause as in the previous example. The farmers grant James permission to enter their land to plant trees and will also contribute money to finance that planting. In return, the farmers will obtain a share of the proceeds of selling the ACCUs plus interest on their money.

This aggregation arrangement is similar to how other managed investment schemes operate – the farmers are earning a return on their investment, rather than merely contributing carbon abatement. The arrangement does not benefit from the proposed exemption as the farmers are contributing both land and money for the aggregator to undertake carbon abatement.

Therefore, James' business must hold an AFSL authorising it to act as a responsible entity and must meet the net tangible asset requirements applicable to responsible entities.

DISCUSSION QUESTIONS

Question 4 Is the proposed exemption appropriately drafted? Does it permit aggregation to take place in an efficient and effective manner?

Question 5 Are there other aggregation arrangements which should be exempted from regulation as a MIS? What are the benefits of these arrangements over arrangements within the scope of the exemption as presently drafted?

Question 6 Is the exclusion from the exemption for aggregation arrangements for a predominantly investment purpose sufficiently broad?

4.3 General Definition of Financial Product

The Act defines a financial product as a facility through which, or through the acquisition of which, a person does one or more of the following:

- makes a financial investment;
- manages financial risk; or
- makes non-cash payments.

Without amendment, aggregation arrangements and carbon abatement contracts may fall within this general definition (in addition to falling within the definitions of 'managed investment scheme' or 'derivative'). Both aggregation arrangements and carbon abatement contracts may be considered to be used for financial risk management purposes and hence within the scope of the general definition.

To provide certainty for ERF participants, the draft regulation also exempts eligible aggregation arrangements and carbon abatement contracts from the definition of 'financial product'.

4.4 Australian Carbon Credit Units (ACCUs)

Sub-regulation 7.1.07I(2) of the Corporations Regulations specifies that ACCUs are financial products, so persons carrying on a business of providing financial services in relation to ACCUs would be required to hold an AFSL.

For example, many activities such as trading in ACCUs on behalf of others, brokering trades of ACCUs between other parties in the secondary market, making a market in ACCUs or operating a financial market in ACCUs are similar to financial services provided in respect of other financial products, such as shares or equity derivatives. It is therefore appropriate to subject these activities to the same regulatory regime, namely the financial services provisions in Chapter 7 of the *Corporations Act 2001*. However, persons trading in ACCUs on their own behalf would not be required to hold an AFSL.[2]

This means that activities in a secondary market for ACCUs may be regulated by the corporations law. Because these activities are similar to financial services already provided in respect of other financial products, it is likely existing financial services firms would provide financial services in respect of ACCUs – including those who are already authorised to provide financial services with respect to ACCUs. The additional compliance burden for existing firms is likely to be low, particularly in light of the potential risks to consumers of these financial services.

The Government recognises that some activities provided in respect of ACCUs may fall within the definition of financial services but for which financial services regulation may be inappropriate. The Government is therefore considering whether exemptions are required for certain financial services provided in respect of ACCUs – as discussed below.

5. Financial Services

5.1 Financial Advice

5.1.1 What is financial advice?

Financial advice, known as financial product advice under the Corporations Act, is defined as a recommendation or a statement of opinion that is intended to influence a person in making a decision in relation to a particular financial product or could reasonably be regarded as being intended to have such an influence.

5.1.2 Role of carbon service providers in providing financial advice

Carbon service providers assist ERF participants in making a bid during ERF auctions by providing information and advice. This includes regulated financial advice and other advice of a technical and non-financial nature (technical advice), which is not regulated under the corporations law.

2 Sub-section 766C(3) provides that a person is not considered to be 'dealing' in a financial product if the person deals on their own behalf (whether directly or through an agent or other representative). Dealing, as defined in s 766C, includes acquiring or disposing of a financial product – that is, buying or selling ACCUs.

For example, a carbon service provider may provide technical advice in relation to the costs of a project, the number of ACCUs that the project may generate, and the operational risks associated with the project. Such advice requires specialist expertise that financial advisers would not necessarily have, including in relation to methodologies for calculating how many emissions reductions would be generated by a project. This technical advice does not constitute financial advice. That same carbon service provider may also provide financial advice by calculating the cost of producing each ACCU and recommending a price to bid into an ERF auction.

5.1.3 Proposed exemption for incidental financial advice

The Government considers that persons providing financial advice in relation to ACCUs should generally be regulated like other financial advisers. However, in some circumstances, the financial advice regulations may be inappropriate. For example, providing financial advice which is minor and provided together with technical project advice may trigger corporations law regulatory burdens, which are disproportionate to the risks to project proponents posed by that advice.

A targeted exemption for incidental financial advice in relation to ERF processes is appropriate given that it is more efficient and cost-effective for carbon service providers to provide minor and incidental financial advice than to separately hire a specialist financial adviser. Given the limited range of financial advice they generally provide, licencing under the AFSL regime may not be appropriate for carbon service providers whose business does not primarily involve providing financial advice.

Example 4: Carbon service provider

A carbon service provider named Alan assists Hans in making his ERF bid. Alan makes inquiries of each farmer – for example, how many trees they would plant, about the soil conditions and so on. Alan then applies the relevant CFI methodology to calculate how many ACCUs are expected to be generated. Alan also asks each farmer how much it would cost to plant those trees. From this, Alan can calculate how much it would cost to produce each ACCU. Alan provides a report to Hans including all this information, and concluding that it would cost $10/ACCU and that Hans should bid $12/ACCU to earn an appropriate return on investment and to provide a buffer against operational risks.

Because ACCUs are financial products, Alan could, if no exemption is provided, be considered to be providing financial advice to Hans by advising what price he should bid. Although Hans could have asked a professional financial adviser to give him this advice separately, it would be more efficient for Alan to do so since he was already familiar with each farmer's operations and already had the requisite information and required expertise.

The exemption would cover Alan's activities. The financial advice he provides is incidental to the main technical advice that he provides, namely, applying the CFI methodology to calculate how many ACCUs would be generated from the tree plantations. Therefore Alan's business would not be required to hold an AFSL.

DISCUSSION QUESTION

Question 7 Is proposed exemption for financial advice which is incidental to technical advice appropriately drafted?

5.2 Dealing

5.2.1 What is dealing?

Dealing is a broad term which includes issuing, buying and selling financial products. The Act defines dealing as:

- applying for or acquiring a financial product;
- issuing a financial product;
- in relation to securities or managed investment interests--underwriting the securities or interests;
- varying a financial product; and
- disposing of a financial product.

Arranging for a person to engage in such conduct is also considered dealing.

A person who deals on their own behalf is not considered to be dealing, unless they are an issuer of that product.

5.2.2 Is a targeted exemption required for aggregators dealing in ACCUs?

Generally, dealers in ACCUs should be required to hold an AFSL. They conduct broking activities whose risk profile is similar to broking in respect of other financial products. Aggregators who engage in these sorts of broking activities should be required to hold an AFSL. However, aggregators should not be required to hold an AFSL merely for engaging in ordinary aggregation activities. The Government is seeking views on whether aggregators engage in activities regulated as dealing in the ordinary course of their business and whether a further exemption is required.

Where the aggregation arrangements are such that the site owners have a beneficial interest in, or have their entitlements depending on, the ACCUs generated by the project by virtue of their entitlement to all or part of the proceeds from the sale of those ACCUs, the aggregator may be dealing on behalf of those site owners when he enters into ACCU sales contracts.

Although carbon abatement contracts are a kind of ACCU sales contract, under the proposed exemption, entering a carbon abatement contract is not regarded as dealing.

However, aggregators may enter other contracts to buy or sell ACCUs. For example, they may buy or sell ACCUs on a secondary market if the aggregation generates more or less ACCUs than required under the carbon abatement contract. This would require an AFSL if the aggregator is considered to be buying or selling those ACCUs on behalf of the site owners.

An aggregator could be provided an exemption for dealing in an ACCU on behalf of a site owner if that ACCU was issued to the aggregator in recognition of carbon abatement (or means of undertaking carbon abatement) contributed by that site owner.

DISCUSSION QUESTIONS

Question 8 Could aggregators efficiently adopt a model in which they did not engage in activities considered to be dealing on behalf of others for the purposes of the corporations law?

DISCUSSION QUESTIONS (continued)

Question 9 Is an exemption required from dealing in relation to ACCUs?

Question 10 Is the potential exemption for aggregators outlined above appropriate?

5.3 CUSTODIAL AND DEPOSITORY SERVICES

5.3.1 What are custodial and depository services?

A person providing custodial and depository services holds assets on trust for or on behalf of a client.

5.3.2 Is a targeted exemption required for aggregators providing custodial and depository services for ACCUs?

As with dealing, aggregators generally should not be required to be licenced as providers of custodial or depository services if the holding is part of an aggregation arrangement and the custody is for relatively short periods. Aggregation arrangements differ from most custodial services which are typically provided on a longer-term basis for persons who have a legal or beneficial entitlement to the assets being held.

In the course of operating a scheme that is an aggregation arrangement, aggregators will at some point hold ACCUs issued to them by the CER. These ACCUs may be held only for a short period of time prior to re-delivery under the ERF contract or sale to another person or they may be held for a longer period of time if, for example, the delivery obligations under an ERF contract are timed to be some time well after the issuance of those ACCUs.

An aggregator may be considered to be, for the purposes of the corporations law, to be providing custodial services on behalf of the site owners, if the site owners have a beneficial interest in, or their entitlements will depend on the ACCUs generated by the project by virtue of their entitlement to all or part of the proceeds from the sale of those ACCUs.

The Government is therefore seeking views on whether aggregators could efficiently adopt a model in which they did not engage in activities considered to be providing custodial and depository services for the purposes of the corporations law.

An aggregator could be provided an exemption for providing custodial or depository services in relation to an ACCU on behalf of a site owner if that ACCU was issued to the aggregator in recognition of carbon abatement (or means of undertaking carbon abatement) contributed by that site owner.

DISCUSSION QUESTIONS

Question 11 Could aggregators efficiently adopt a model in which they did not engage in activities considered to be providing custodial or depository services?

Question 12 Is an exemption required for providing a custodial or depository service in relation to ACCUs?

Question 13 Is the potential exemption for aggregators outlined above appropriate?

5.4 Making a market

5.4.1 What is making a market?

A person makes a market in ACCUs if they regularly state the prices at which they propose to buy or sell ACCUs on their own behalf and they have a reasonable expectation that they will be able to regularly effect transactions at the stated prices.

5.4.2 Is a targeted exemption required for aggregators making a market in ACCUs?

Generally, a person making a market in ACCUs should be regulated in the same manner as other market makers. The Government is seeking views on whether targeted exemptions should apply in certain circumstances.

It is possible for aggregators to adopt a market-making model. The Government is seeking views on why such an aggregator should not be regulated in the same manner as other market makers. In the absence of a compelling reason for an exemption, no exemption should be granted.

DISCUSSION QUESTIONS

Question 14	Is an exemption required to provide that an aggregator making a market in ACCUs or ACCU derivatives to a client it is not making a market for a financial product?
Question 15	Should any other exemptions be provided for particular financial services provided in respect of ACCUs?

5.5 Alternative Targeted Consumer Protections

As outlined above, the Regulation will have the effect that most aggregators and carbon service providers will not be required to hold an AFSL or provide a Product Disclosure Statement to retail clients. Consumers involved in the ERF will instead have the benefit of alternative targeted consumer protections, including guidance about aggregation.

Firstly, ACCUs will still be considered financial products. Secondly, the changes to the Regulations are targeted to the particular ERF activities outlined above. The Regulations will retain a number of regulatory requirements on activities outside the scope of the changes.

To manage any residual risks following these exemptions, the Department of the Environment, in consultation with Treasury and the Australian Securities and Investments Commission, is developing a standardised disclosure document which would highlight the risks and benefits generally associated with participating in an aggregated project. The Department is also developing standardised aggregation contracts which would include some basic protections for smaller parties to the contract. All other Commonwealth, State and Territory legislation and regulations regarding business entities will continue to apply.

The Government will consult on these documents separately.

DISCUSSION QUESTIONS

Question 16 Will an appropriate level of consumer protection be achieved by the alternative targeted protections discussed above?

Question 17 Should the regulation require persons benefiting from the exemptions to provide the standardised disclosure statement to ERF participants?

Question 18 What other protections might be necessary?

6. GLOSSARY

- **Aggregator**: a project proponent which makes a bid during an ERF auction on behalf of discrete or separate emissions abatement activities.
- **Aggregation arrangement**: an arrangement under which aggregation occurs. The arrangement is usually governed by an aggregation contract, which governs the rights of the parties and under which the site owners grant the site owners a legal right to carry out the abatement project.
- **Carbon abatement contract**: a contract between the Clean Energy Regulator and a project proponent which successfully bids in an ERF auction. It sets out the delivery schedule for ACCUs and the price for those ACCUs.
- **Carbon service provider**: Carbon service providers assist ERF participants in making a bid during ERF auctions by providing information and advice, including both financial product advice and technical project advice.
- **Project proponent**: the person who makes a bid during an ERF auction.
- **Site owner**: the owner of a site on which carbon abatement activities will take place; a member of the aggregation arrangement who is not the aggregator.