

Submission to the Australian Government's Nature Repair Market Bill

The Australian Sustainable Finance Institute | February 24, 2023



Introduction

The Australian Sustainable Finance Institute (ASFI) welcomes this opportunity to make a submission on the design and development of the Nature Repair Market legislation, and specifically to comment on the exposure draft of the Bill (the Bill).

ASFI represents Australian financial institutions – including major banks, superannuation funds, insurers, asset managers, and financial services firms – that are working to align the Australian financial system with a sustainable, resilient, and inclusive Australia. ASFI members collectively hold over AU\$18 trillion in assets under management and are committed to allocating capital in a way that supports positive social and environmental outcomes.

Key Messages

ASFI supports the government developing a robust, high-integrity market framework that would enable funding and investment in nature protection, restoration, and enhancement, with the ultimate objective of achieving net positive gains for Australia's natural environment.

The development of a nature market framework is necessary but not sufficient to redirect financial flows towards nature positive outcomes. Equally important to determining whether the nature repair market will ultimately drive nature positive outcomes aligned to the Bill's objectives and catalyse demand for nature repair markets and activities are:

- The **enabling regulatory environment** which needs to be established, including the combination of effective environmental protection regulation; clear legislated conservation and restoration targets in line with the new Global Biodiversity Framework (GBF); explicit links between the GBF targets and the Nature Repair Market activities; support for nature-related corporate disclosures; and the use of blended finance mechanisms to de-risk and crowd in private capital at scale.
- The **design features of the market**, which should be robust, high-integrity, transparent, and usable.
- Careful consideration of the **market "uses"** of the nature repair market units, particularly while the market is in its nascency and market demand for investment in nature positive outcomes is shallow.



Enabling Environment

ASFI supports the implementation of the recently agreed global targets on environmental protection and restoration set out in the Kunming-Montreal Global Biodiversity Framework (GBF). These targets help capital markets to align activities and investments with clear outcomes namely:

- protecting 30 per cent of land and seas by 2030 and bringing the loss of areas of high biodiversity importance to zero;
- restoring at least 30 per cent of degraded landscapes and seas by 2030;
- recognising the crucial role Indigenous peoples have in the protection of nature and recognising and respecting their rights including over their traditional territories.

To help catalyse private sector investment in Australia to restore and protect nature, these global targets need to be translated and embedded into domestic legislation and policies. This should be done through:

1. Enshrining in legislation and make legally binding the commitment to protect 30 per cent of land and seas by 2030 and restore 30 per cent of degraded landscapes and seas.
2. Ensuring that the proposed reforms to Australia's environmental protection laws effectively deliver on the GBF targets and are considered in the development of National Environmental Standards under the EPBC Act reforms. The GBF targets should be key considerations in the decision-making framework for environmental approvals and embedded in Regional Plans, which should include crucial information including, identifying areas of high biodiversity importance, and areas earmarked for protection and restoration.
3. The implementation of Target 15 of the GBF by the Australian Government to "take legal, administrative and policy measures to encourage and enable business, and capital markets to regularly monitor, assess and transparently disclosure their risks, dependencies and impacts on biodiversity, including with requirements for all large as well as transnational companies and financial institutions along their operations, supply and value chains and portfolios." This should be progressed in line with international standards through the evolving ISSB sustainability baseline standards and the TNFD framework.
 - In addition to continuing to support the development, understanding and uptake of TNFD in Australia, government should look to develop bespoke guidance in particular areas, especially as they relate to broader sustainability reporting when this is introduced – in particular, First Nations rights/protections and participation.

- Support and inform the development of disclosure standards, supervisory reporting and other prudential policies and governance of financial market conduct, including addressing greenwashing.

4. As part of the Australian Government's sustainable finance strategy, government should:

- Invest in the dissemination and availability of robust and credible data to inform climate and nature risk and opportunity disclosures at appropriate level and granularity, and support markets to value and invest in natural capital assets.
- Support the RBA's engagement with the Network for Greening the Financial System (NGFS) taskforce on nature-related risks, including the development of nature-risk scenarios. This will help ensure that global nature-risk scenarios being developed are informed by Australian experiences and expertise.
- Develop Australia specific nature-risk scenarios for key areas of national significance, for example the Great Barrier Reef and the Murray-Darling River system, building on the oceans and regional ecosystem accounts work undertaken by the department.
- Support the development over time of technical criteria for environmental objectives (biodiversity and ecosystems across land, water, and seas) in the forthcoming Australian Sustainable Finance Taxonomy.

5. Design and provide catalytic investment in blended finance models to de-risk and crowd in significant private capital to fund the recovery of nature. Blended finance can catalyse investment in high-integrity nature projects with ongoing revenue generation from ecosystem services such as carbon sequestration, coastal resilience against storm surges, biodiversity and water quality. Government backed blended finance mechanisms can aggregate key projects to an investible level, lower transaction costs and reduce risk to a point where institutional investors are able to participate.

- Government backed blended finance models can provide a template and track record for private sector investment in nature recovery at scale for others to follow.¹

Market Design

To ensure participation from both capital markets and supply-side project proponents, the Nature Repair Market should embody the key design features of:

- **Integrity:** The regulatory framework in place prevents fraud and manipulation, ensures accountability, upholds scientific integrity and prevents conflicts of interest.
- **Transparency:** Like other trading markets, buyers and sellers need to be accessible to one another (public register), the market should be regulated to ensure fair conduct and good trade practices, and pricing should be transparent.
- **Information symmetry:** all participants have the same information about the assets being traded. Market information should be readily available. Transactions should be traceable.

Integrity

Governance

ASFI supports how the Nature Repair Market Bill exposure draft establishes clear separation of powers, accountability and transparency in decision making regarding the development of methods by the relevant department, the independent assessment of methods by the Nature Repair Market Committee, the determination of methods by the Minister on the advice of the Nature Repair Market Committee, and regulation of the market by the Clean Energy Regulator.

ASFI notes that the Nature Repair Market Committee are appointed on a part time basis. Drawing on learnings from the Emissions Reductions Assurance Committee under the Emissions Reduction Fund, it is imperative that the Nature Repair Market Committee is provided with sufficient secretariat support to fulfill their statutory obligations to properly assess the biodiversity integrity of new methods.

ASFI supports the balance of skills used to determine eligibility of a Nature Repair Market Committee member, however, the way the Bill is currently drafted, the Minister has the discretion to appoint members with experience, standing and knowledge in any one of the listed skills. The Minister could appoint several members to the Committee that possess a narrow representation of the listed skills. It is important to ensure that a balanced representation of the skills listed is represented on the Committee at any given time. Accordingly, when appointing new members, the Minister should be obliged to ensure that the members collectively represent a balance of skills listed in the Bill and there is not an over-representation of one skill on the committee at any given time.

Legislative Reviews

ASFI supports the five yearly reviews of the Act to ensure that it is achieving its objectives.

- It is unclear from the Bill who will undertake the review and how the review process will be established. It is imperative that the review of the operation of the Act is undertaken as part of an independent and transparent review process.
- To ensure ongoing market trust and integrity in the scheme, ASFI recommends that the effectiveness of auditing, assurance, monitoring and compliance of activities be explicitly identified as part of the periodic review of the operation of the Act.

Environmental Integrity Standards

ASFI supports the biodiversity integrity standards listed in the Act, in particular the inclusion of both protection and enhancement activities and the requirement that methods must be measurable, assessable, and verifiable.

- ASFI recommends more explicit alignment of the language used in the biodiversity integrity standards set out in section 57, with the objectives of the Bill. In particular, drawing a clear link between the standards and meeting Australia's international obligations under the GBF, with the primary objective of driving net gain for nature.
- Currently there is no definition of "enhancement", so market participants are unable to assess whether a minimum level of nature gain will be required in the development of methods.
- It is imperative for the perception of legitimacy and integrity of the scheme that all methods established under the Bill have a baseline level of nature gain or additionality. There are several internationally recognised examples of defining additionality for nature markets that the Bill can draw from.²

Transparency and Information

Biodiversity methods, certificates, and market comparability

ASFI recognises the significant complexities that arise from an attempt to unitise nature for the purpose of comparing, pricing and trading. Balancing simplicity with scientific credibility is key to determining market participation from both the supply and demand side. If the scheme is too complex and costly it will deter both supply and demand. Likewise, if the market perceives that the scheme is not scientifically credible, it will not participate in it.

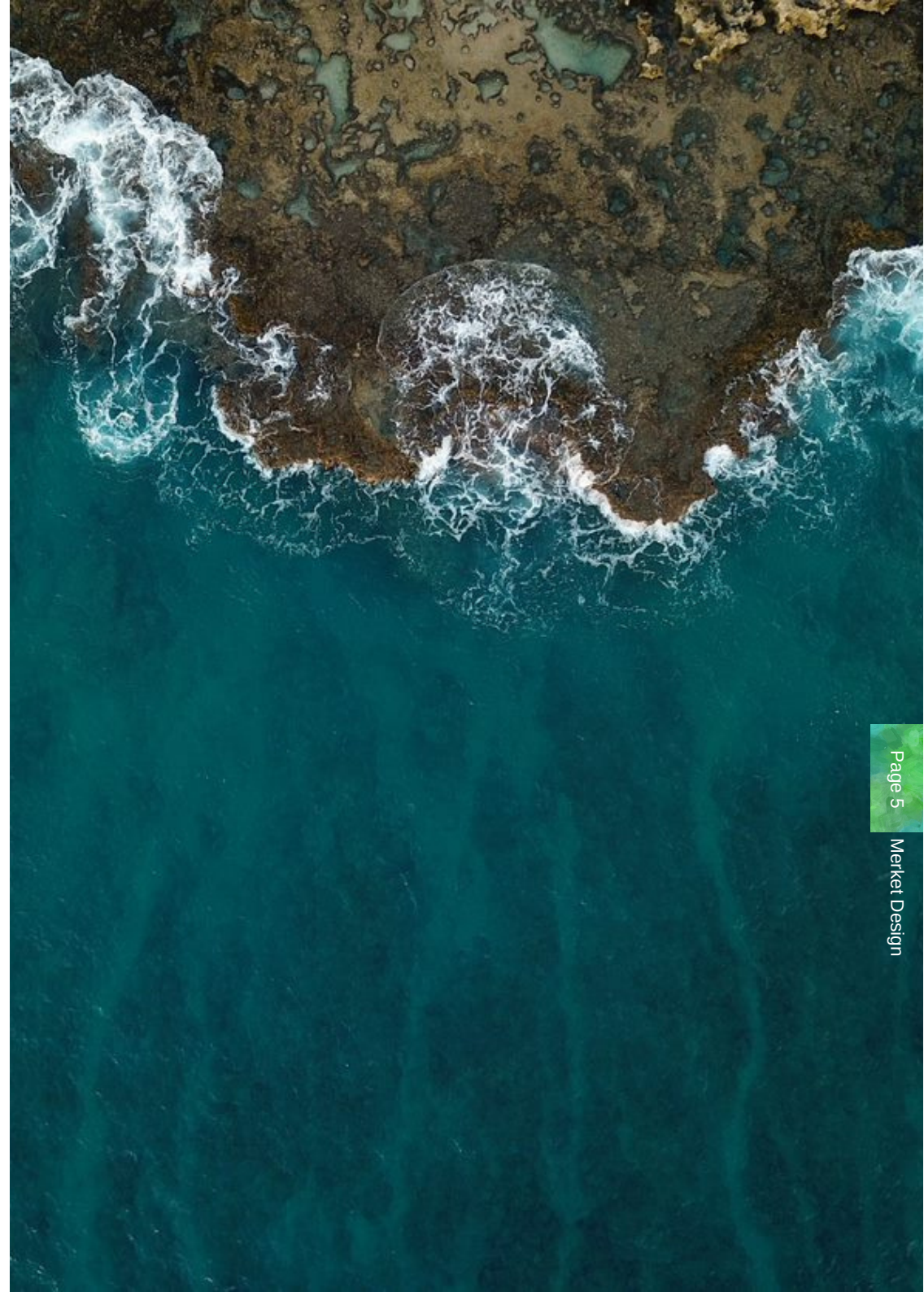
ASFI supports the approach that certificates are customised to the project, to avoid the complexities of unitisation and prevent artificial equivalence. However, market

transparency and comparable information are prerequisites for private capital participation in markets. It is important that the template of the biodiversity certificate is designed and produced in a way that enables the information in the certificate to be easily understood and comparable with other certificates. Standardisation of information is key to market engagement.

- ASFI supports the proposed Biodiversity Assessment Instrument to address the lack of universal comparison. There should be full transparency regarding the methodologies used for the comparisons in the Instrument. These methodologies should be based on best-practice science and should be produced to be easily accessible and understood by the market.
- Biodiversity methods should be underpinned by robust measurement standards that are integrated across national accounting frameworks, and complemented by project design methodologies that achieve ambitious and enduring outcomes.
- Biodiversity methods under the scheme must prioritise biodiversity outcomes (increases and improvements in biodiversity) not activities (number of invasive animals controlled, hectares of protected land). The market will not view the method as having integrity if the outcome is not clearly defined and can be measured and verified.

ASFI supports the publication of biodiversity certificates and the establishment of a public register of certificates.

- The public register must be easily accessible and searchable and should reflect historical transaction data, as well as keep a log of amendments or changes to the certificate for tracing purposes and avoidance of double counting certificates across the primary and secondary market.
- This register will need to include guidance for those purchasing primary certificates as well as secondary certificates which may have different properties.



Market Uses

Use as offsets in compliance market

In the absence of substantial private sector demand for investment in nature positive outcomes in short-to medium term, the most significant source of demand for credits is likely to come from offsets required under the EPBC Act and other state-based compliance markets.

There are valid scientific concerns regarding whether species, which are heavily location-dependant can ever be said to be equivalent across regions or whether the destruction of intact habitats can be adequately offset by establishing or enhancing another habitat. This is why compliance markets ordinarily require additional scrutiny and complexity to compensate for the destruction of an existing habitat. However, many of the features present in other compliance markets are not featured in the Bill.

By Definition, an offsets market, if designed and functioning correctly, should maintain the status quo for nature by offsetting any losses that are authorised under law. Given the current state of the environment, this is not a desirable outcome and not aligned with the Bill's primary objectives of achieving Australia's international obligations of net nature gain and increased protection.

In the Government's Nature Positive Plan, published in December 2022, it recognises that current offset arrangements are contributing to environmental decline, and commits to reforming the offset arrangements to ensure they deliver gains for the environment. The plan proposes to do this by ensuring among other things that "offsets will need to be identified within the region that deliver a net gain for the imperilled plants or animals".³

As highlighted above, the Bill does not define "enhancement" as requiring nature gain/additionality, nor does it define net-nature gain. If the nature repair market scheme is used as a source of offsets in compliance markets, serious consideration should be given to the additional regulatory safeguards that will need to be put in place to ensure net gains for nature, including a clear definition of the concept of net gain and embedding it into the environmental integrity standards. Other guardrails that could be put in place, where necessary in the Bill, or as part of the reformed offsets arrangements are:

- Ensuring net gain by mandating that credits are for improvements beyond business-as-usual baseline.
- Continuing to ensure ecological equivalence between the area being imperilled and

the offset credit, and the development of standards for ongoing monitoring and reporting of the extent and condition of the project to ensure not only ecological equivalence of the project, but that the condition and health of the project reaches a state of equivalence of the area being offset.

- Mandating that the quantity of credits required as offsets is a multiple of the biodiversity being imperilled or destroyed, with the multiple increasing based on the biodiversity value.
- At least in the near term, where private demand is weak, offsets could be restricted to new projects only (primary market). This would assist in the generation of additional activities under the scheme to help achieve net gains for nature.
- Certificates used for offsets must be retired to ensure there is no double counting, or claims of nature gains, where no gains have in fact occurred.
- The performance period for offsets projects should be set appropriately, and robust frameworks should be put in place to ensure the long term financial and ecological sustainability of credit projects.

The review of the effectiveness of the NSW Biodiversity Offset Scheme, released in 2022, identified several factors that have led to a net loss for nature, due to biodiversity gains from the scheme not being sufficient to offset the losses resulting from development. Key issues with the scheme included:

- A mismatch between supply and demand, and lack of information about supply, demand and price.
- A lack of frameworks to ensure the financial and ecological sustainability of biodiversity stewardship sites.

The nature repair market scheme, as proposed in the current bill, is likely to face many of the same issues at least in its initial phases and should as a starting point incorporate the learnings from the review of the NSW Biodiversity Offset Scheme.

Overall market demand

It is unclear to ASFI where the private demand for nature repair credits beyond philanthropy will come from in the short to medium term, especially in the absence of the broader enabling environment and catalytic blended finance models set out above.

Corporate reporting on nature-related risks and dependencies could drive demand over the medium-to-long term, however nature credits will only ever be one part of private sector response to nature-related risks.

As with investor expectations in relation to climate change, investors will seek corporate responses that first mitigate and avoid future impacts on nature, with clear corporate plans to transform harmful business models, and lastly where harm cannot be avoided and as a temporary and interim solution to transforming business practices, it may be

acceptable for corporates to invest in nature credits to mitigate impact.

For the nature repair market to be sustainable and enduring, long term determinants of demand need to be identified and supported. In the absence of strong demand, the price for credits will not be sufficient to incentivise supply or to compensate suppliers for ongoing maintenance of projects and participation in the scheme.

ASFI has identified key enablers (set out above) to help drive demand. In addition, the government should seek to closely align the nature repair market with the carbon market or other established ecosystem markets.

Government could also use its balance sheet to strategically co-invest in the high value/high priority biodiversity co-benefits of carbon projects to leverage existing (and growing) private demand for carbon markets, socialise biodiversity credits with a broad range of market participants and achieve positive biodiversity outcomes.

Endnotes

[1] See example of the “Big Nature Impact Fund” established by the government of the United Kingdom and managed by investment manager Federated Hermes. <https://www.gov.uk/government/news/update-on-the-big-nature-impact-fund>.

[2] World Economic Forum, High-level governance and integrity principles for emerging voluntary biodiversity credit markets, Consultation paper, December 2022. https://www3.weforum.org/docs/WEF_Biodiversity_Credits_Markets_Integrity_and_Governance_Principles_Consultation.pdf.

[3] Department of Climate Change, Energy, the Environment and Water, Nature Positive Plan: better for the environment, better for business, December 2022. <https://www.dcceew.gov.au/sites/default/files/documents/nature-positive-plan.pdf>.