17 July 2024

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The Treasury
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Sent via email: HydrogenProductionTaxIncentive@treasury.gov.au

FUTURE MADE IN AUSTRALIA: HYDROGEN PRODUCTION TAX INCENTIVE

Dear Mr Gebers,

The Chamber of Minerals and Energy of Western Australia (CME) is the peak representative body for the resources sector in Western Australia. CME is funded by member companies responsible for 20 per cent of Australia's corporate income tax receipts in 2022-23.[1]

In 2022-23, the WA resources sector accounted for 65 per cent of Australia's resources exports,[2] half of Australia's resources capital expenditure[3] and 53 per cent of Australian resources employment.[4] Within this membership, interests in hydrogen development range from project proponents to major infrastructure providers (e.g. port, pipeline and network providers) to potential end-use customers (e.g. iron ore, bauxite-alumina, ammonia and other industrial producers)[5] and energy providers across both domestic applications and export opportunities.

Overview

Hydrogen is a potentially significant contributor to Australia's net zero transition and almost a quarter of Australia's planned and operating hydrogen projects are in WA.[6] Hydrogen could also create economic diversification opportunities through its potential use in the production of 'green' iron and steel, as well as for export markets.

However, numerous barriers to a successful hydrogen industry will require considered and substantive support from the government to stimulate both supply *and* demand. On the supply side, CME believes government support should focus on developing supply at sufficient scale to be internationally competitive in the medium to longer term, with the commercial viability of low or zero-carbon hydrogen a key barrier to industry development. This will likely involve strategic investment to reduce project risk and costs in the hydrogen supply chain, essential infrastructure, and manufactured componentry, and support innovative commercial models.

CME set out its broad position on hydrogen in its Toward Competitive Clean Hydrogen[7] position paper in 2021. We welcomed the Hydrogen Production Tax Incentive (HPTI) announcement under the umbrella of the *Future Made in Australia* plan as part of the 2024-25 Budget. We are grateful for the opportunity to provide feedback to the Treasury on the specific details, having sought comments from members with an expressed interest in hydrogen.

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[1] Includes company tax, fringe benefits tax, petroleum resource rent tax and excise duty. Commonwealth of Australia, Final Budget Outcome 2022-23, The Treasury, 22 September 2023, Note 3: Taxation revenue by type, p 39.
[2] Government of Western Australia, 2022-23 Economic Indicators Resource Data File, Department of Energy, Mines, Industry Regulation and Safety (DEMIRS), 9 January 2024. Australian Bureau of Statistics (ABS), 5368 International Trade in Goods, Table 32a.
[3] Investment refers to capital expenditure as measured by gross fixed capital formation, current prices. ABS, 5220 Australian National Accounts: State Accounts, Table 25. ABS, 5206 Australian National Accounts: National Income, Expenditure and Product, Table 34.
[4] ABS, 6291 Labour Force, Australia, Detailed, Table 5.
[5] Reflecting the opportunity of decarbonising iron and steel, aluminium, other metals, chemicals and liquefied natural gas. Australian Industry Energy Transitions Initiative (Australian Industry ETI), Pathways to industrial decarbonisation: Positioning Australian industry to prosper in a net zero global economy, phase 3 report, February 2023.
[6] 24 of 102 active projects, with a further 12 archived, CSIRO Hydrogen Projects Spreadsheet derived from HyResource Project, Active Webpage last updated 2 July 2024.
[7] Available on CME's website.

Overall comments

CME supports the proposed tax incentive to stimulate investment in the growth of the supply of renewable hydrogen. While we are of the view that the HPTI of $2/kg *alone* will not in itself close the completeness gap and lead to large-scale growth of the hydrogen economy, a simple, targeted tax incentive will play a key role in unlocking investment. Coupled with a range of other forms of public support, the HPTI will play an important role in projects as they compete for international capital, particularly against other markets where similar incentives are already being made available.

1. Eligibility Criteria

CME concurs strongly with the Treasury's principle of keeping the administration of the HPTI as simple as possible. We agree with the observation that international experience has shown that complex eligibility and compliance rules can disadvantage early-stage projects in the nascent hydrogen market. We largely agree with the eligibility provisions set out in the consultation.

CME notes the proposed cut-off for final investment decisions (FID) set at 30 June 2030. However, like all energy projects, hydrogen will require comprehensive infrastructure planning and timely approval processes across different levels of government. Many projects are likely to be conditional on the build-out of renewable generation capacity, and in WA, in particular, the build-out of transmission infrastructure. There is therefore a risk that all but the most advanced projects might be unable to reach FID before 30 June 2030.

For large-scale projects, even those that do reach financial close in time might not be able to commence production until the mid-2030s. With the incentive period ending on 30 June 2040, this means the incentive would be available for these projects for significantly less than the intended ten-year window. We therefore strongly recommend that the Treasury considers extending the 2030 and 2040 cut-off dates and actively review the pipeline of projects on which the $6.7 billion Budget allocation was made to ensure that projects are not disadvantaged, particularly where there are delays outside proponents' control.

For those projects that are advanced, we would recommend bringing the scheme start date of 1 July 2027 forward.

We also note the consultation suggests the $2/kg tax offset will not be indexed for inflation. We recommend that the Treasury reconsiders this, noting that there is a risk that the $2 rate could be significantly eroded over the period that the tax credit will be made available. This is particularly important given that the $2/kg rate is substantially less than the US Section 45V tax credit of US$3 (approximately A$4.5), which is available for the lowest-emission production in the US.

2. Eligible Production

In line with our comments above on ensuring that the HPTI is kept administratively simple, CME welcomes the proposal not to require hourly time-matching against renewable generation and to use the Guarantee of Origin (GOO) scheme to ensure compliance on an annual basis. This will be a key way to reduce project costs and improve the competitiveness of Australia's hydrogen economy.

CME agrees with the proposal that the incentive should be made available only to those projects that are able to demonstrate a physical grid connection to renewable generation so that grid-connected hydrogen production does not result in a net increase in the carbon intensity of the grid. This light-touch requirement is sufficient, particularly given that projects will be largely operating in the 2030s when, Australia-wide, 82% of electricity is intended to be renewable. However, any further additionality requirements should be considered with caution: WA's grid arrangements are different to the NEM in that they are localised and dispersed. Grid systems in the state need significant, rapid investment to improve capacity to accommodate increased renewable build-out, particularly in the South West and North West Interconnected Systems.

We also note the Treasury's proposal to limit eligibility to projects that are above 10MW equivalent nameplate capacity, verified by the Guarantee of Origin scheme. While we agree with the HPTI's objective of growing at-scale production of hydrogen, we note that this level would prevent small-scale hydrogen production, for instance, for passenger or heavy-duty transport, or energy storage and generation on microgrids. We therefore suggest that Treasury open the scheme to projects above a minimum threshold of 1MW. While these projects might not be operating 'at scale,' our members believe that these should be eligible for support, which will be particularly important to support localised, off-grid projects in WA. We agree that there should be no capacity cap for the incentive.

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CME's membership represents diverse opportunities for low-carbon hydrogen production. We note that the Treasury intends for the HPTI to bring forward production of 'renewable' hydrogen, with a limit of 0.6kg of CO_2 emitted per kilogram of hydrogen. For the purposes of supporting electrolytic hydrogen powered by renewable electricity, this intensity limit is appropriate.

However, we note that other jurisdictions are providing government support to unlock opportunities for at-scale low-carbon hydrogen production from other production pathways, with the intention to bring forward demand and stimulate global market expansion. Notably, the US has a sliding scale to support other forms with a higher emissions intensity than electrolytic hydrogen, and other markets like the UK provide incentives for hydrogen below 2.4kg CO_2e, and below 3.4 kg of CO_2e in the EU and Japan (on a full life-cycle approach). To ensure that Australia is well-placed gain early mover advantage in the global hydrogen economy, **CME recommends that government should consider support to other production pathways, including CCUS-enabled production.**

CME welcomes the proposal to allow the HPTI to be awarded for hydrogen production regardless of end use, including for export to other markets. This will help establish new, long-term trading opportunities for Australian hydrogen as the global market matures.

3. Administrative Arrangements

CME's members agree with the principles outlined in the consultation, including the use of the GOO scheme as a light-touch means to ensure compliance. As noted above, a streamlined and efficient regime will be key to ensure that Australia remains competitive with other jurisdictions that offer similar incentives, so that it is able to establish its hydrogen economy quickly. It will be crucial that the design of the GOO scheme ensures there is no administrative duplication where projects receive other forms of public federal and state funding.

4. Community Benefit Principles

The WA resources sector directly supported 18,712 local businesses, 1,396 community organisations and 78 local governments across Australia.[8] In terms of diversity and inclusion[9], in 2021, the WA resources sector women's workforce representation was at 21.5 per cent, while Aboriginal and Torres Strait Islander peoples' representation was 5.2 per cent. The participation of Aboriginal and Torres Strait Islander people in the WA resources sector was significantly above the 3.3 per cent population share as at the 2021 Census.

It is reasonable for the Australian Government to consider that HPTI recipients should meet certain minimum conditions, subject to certain thresholds. However, the need for annual reporting against those needs to be balanced to ensure the administrative costs of access do not outweigh the benefits. CME recommends that reporting requirements should not duplicate existing reporting requirements (e.g., for Workplace Gender Equality Agency reporting, Payment Times Reporting Scheme and Modern Slavery Statements) and the timing, frequency and content of company reporting should be aligned wherever possible. Also, any minimum conditions should apply at the taxpayer level rather than the facility level. This recognises that individual hydrogen production facilities may face challenges meeting certain criteria, such as minimum trainee, female and First Nations employment, due to their geographical location and the associated availability of housing, transport and labour.

Community Benefits Principles should be consistent with existing requirements under any relevant State Agreements and Australian Industry Participation Plans and reporting disclosures to avoid duplication.

Conclusion

CME welcomes the introduction of an HPTI as a measure to support Australia's net zero future. However, the HPTI alone is unlikely to be sufficient to close Australia's competitiveness gap and stimulate the investment required to develop a sustainable, value-adding and job-creating hydrogen economy. Sustained investment will be required across the full hydrogen value chain to stimulate production, storage and distribution, demand, supply chain growth, and capability development. A basket of measures, including those announced in the

[8] CME Economic Factsheet 2022-23
[9] Diversity and Inclusion in the Western Australian Resources Sector

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Future Made in Australia package and the extension to the Hydrogen Headstart program, should continue to work to address these issues, in tandem with WA Government support.

CME has previously advocated for federal and state governments to work with industry to accurately assess the scale of electricity infrastructure requirements to unlock carbon reductions, including in the hydrogen sector. CME's members strongly support the hub model as a way of improving the bankability of projects, increasing innovation and information sharing, and decreasing costs and waste.

It is also necessary to streamline federal-state approvals processes to provide certainty over approvals processes and timeframes, reduce complexity, reduce costs, and improve efficiency. The provision of shared infrastructure, including well-located, turnkey strategic industrial areas is also critical. Australia also needs to work with our key trading partners to support the development of resilient supply chains and foster demand in new hydrogen markets from which Australia will be well-placed to benefit in the medium to long term.

We thank the Treasury for the opportunity to provide our sector's insights on the issues for discussion and look forward to ongoing engagement on the HPTI and wider support for the hydrogen economy. For further information, please contact Steven Mills, Manager – Climate and Energy, on 0428 920 314 or via email at s.mills@cmewa.com.

Yours sincerely

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