

Climate Change Policies Review – Discussion Paper submissions
2017 Review Branch
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Review of Climate Change Policies – Discussion Paper

The Australian Energy Council (the Energy Council) welcomes the opportunity to make a submission to the Australian Government's Review of Climate Change Policies (the Review).

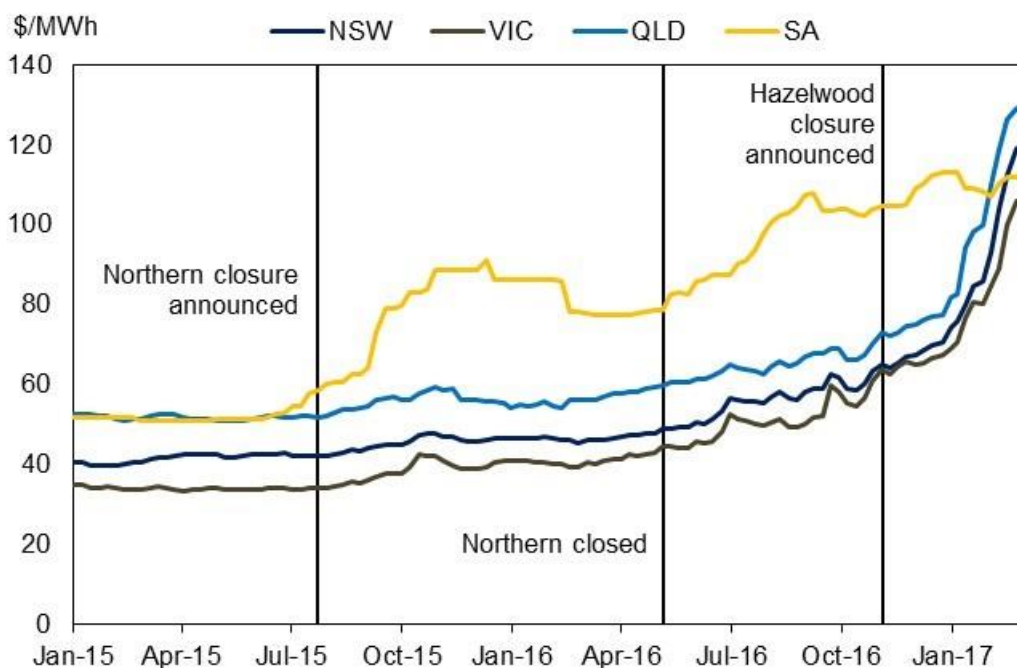
The Energy Council is the industry body representing 21 electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. These businesses collectively generate the overwhelming majority of electricity in Australia and sell gas and electricity to over 10 million homes and businesses.

Long-term goals and stable policies support long-lived investments

A long term goal consistent with the Paris commitment to which the Australian government was a party (i.e. to collectively seek to avoid 2 degree warming) is a useful part of the framework to give clarity to investors in long-lived assets. Policies should be capable of being scalable to contribute effectively to the goal. Australia will be able to meet its 2030 targets more efficiently if the 2030 target is not seen as an end goal in itself, but rather a milestone on the way to deeper emissions reduction over the longer term.

A lack of effective policy consistent with the 2030 target creates uncertainty for investors. Uncertainty ultimately has a cost for customers. This is a contributor to current wholesale prices across the NEM which are higher than historical trends. It is clear that simply forcing in subsidized renewables does not mitigate cost in the long-run. Since 2012 more than 5,000MW of firm generation has left the National Electricity Market (NEM). The reduction in the supply-demand balance and a recovery in demand since 2015 has significantly increased prices in the forward contract market for electricity (refer to Figure 1).

Figure 1: Contract prices in NEM regions, for delivery in CY 2017



Source: NEM Review, 2017

Higher wholesale prices are a signal by the NEM for investors to enter the market and increase supply. Investors have been unable to replace retired generation because of sustained policy uncertainty over the past decade rendering new generation investment currently unbankable. In Australia, the lack of national policy certainty is now the single biggest driver of higher electricity prices. We estimate that the cost of sustained national policy inaction is effectively equivalent to a carbon price of more than \$55 a tonne¹.

New investment will often come from the same sources as existing investment. Accordingly policy design should also account for the impact on existing plant. While decarbonisation logically requires that existing plant will ultimately close, in some cases ahead of what had previously been considered its economic lifespan, unnecessary value destruction should be avoided.

Climate and energy policy need to be better integrated

Climate policy has too often been developed under a different portfolio from the energy portfolio. This has resulted in an approach that has failed to fully consider the consequences of such policy for energy security, reliability and costs. Additionally state-based policies have often failed to consider how they operate within the NEM. There needs to be a clear national pathway in order to persuade state and territory governments that they do not need to have their own climate change mitigation policies.

WA and the Northern Territory remain outside the NEM. Climate policy for the energy sector will need to take account of the specific circumstances of those jurisdictions as well.

A sectoral approach

The electricity sector has a major role to play in Australia's emissions reduction process. As the electricity sector lowers its emissions intensity, abatement opportunities will arise from the electrification of transport and industrial processes. This process will however increase absolute emissions for the sector. A sectoral

¹ Our estimation of this figure can be found at <https://www.energycouncil.com.au/analysis/how-much-carbon-tax-are-you-paying/>

approach that carves up the overall target to individual sectoral targets will need to account for issues such as fuel switching.

The industry remains keen to work with the Government on the development of any sectoral emissions reduction policy. Existing policies applied to the sector are not designed to efficiently reduce emissions. The RET aims to incentivise new generation prior to 2020 but will have limited impact beyond this. The RET has brought on new zero emissions generation, mostly wind, but does not:

- provide an effective price signal of the value of contributions to security of supply;
- does not value low or zero emission plant such as gas, thermal plant with carbon capture and storage, hybrid plant or (potentially) nuclear plant;
- does not provide clear signals for the exit of high-emissions plant
- does not value efficiency gains in existing plant, and;
- has proved to be not flexible to changes in the target.

These factors will all become more important at greater levels of emissions reduction, so while the industry can manage around the existing RET, it is not suitable for further extensions.

The Safeguard mechanism is an effective mechanism for constraining emissions growth but does not provide incentives for emissions reduction, and so is not suitable for ensuring emissions abatement over the long term in its current form.

A role for domestic and international units

The Government's emissions reduction fund (ERF) has created demand for accredited domestic abatement. Given that it is not clear that the Government wishes to fund ERF auctions on an ongoing basis, there is merit in considering the ways such domestic credits could play a cross-sectoral role in future abatement policies. Specifically if any sector is subject to a compliance obligation, then acquiring and submitting accredited domestic abatement units should be a legitimate method of meeting such obligations.

Similarly, credible international units should be allowed to play a role in meeting our commitments, given the global scale of the challenge. How this occurs will depend on specific policy design. The international community will have to consider the ongoing processes for accrediting activities that genuinely contribute to emissions reduction post 2020. Australia should play a constructive role in this process and consider both opportunities to both sell and purchase abatement.

Jobs, investment, trade competitiveness, SMEs and households

Efficient policy will minimize cost impact for customers of all sizes. This will also be the best support for jobs, competitiveness and investment across the economy. An efficient policy is one that harnesses the power of markets and focusses on the outcomes (emissions reduction, while maintaining energy security) rather than technology-specific inputs.

Whilst it is a natural role of governments to be concerned with broader economic outcomes, attempting to design a policy to satisfy too many goals generally results in sub-optimal outcomes.

Leveraging research and development

Research development and demonstration activity (RD&D) is important for uncovering the most effective and efficient solutions to the challenges posed by emissions reduction. This activity requires government support given the difficulties innovators face in recovering investments made at these early stages. We recognise that government funding will be limited, so it is crucial to target it efficiently. RD&D support should not be targeted at deployment, for which we have markets. It should also be targeted at the Australian context. RD&D that results in incremental improvements to the manufacturing of, say solar panels and wind turbines,

is not of obvious relevance to Australia as we are not a manufacturing centre for such products. Instead support should be targeted at areas where Australia has specific strengths that we can exploit through our existing industries and at solving Australian-specific problems. Many of these are in the area of effective integration of existing technologies. In the electricity sector, the new zero emission technologies that are being deployed (solar, wind) are very different in characteristic from the thermal plants they are replacing. This puts parts of Australia at the cutting edge of integration challenges, and is an obvious area where innovation can make a difference.

Any questions about our submission should be addressed to me by email to Kieran.donoghue@energycouncil.com.au by telephone on (03) 9205 3116.

Yours sincerely,



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