

6 July 1998

The Secretary  
House of Representatives Standing Committee on  
Environment, Recreation and the Arts  
Parliament House  
Canberra ACT 2600

Dear Sir,

**Inquiry into the Regulatory Arrangements for Trading in Greenhouse Gas Emissions**

I would be pleased if the attached submission on behalf of the Hydro-Electric Corporation could be put before the Committee at its next sitting for the above Inquiry.

HEC would be pleased to amplify any of the content of its submission or appear before the Committee if required and our contact person is Mr Peter Rayner who can be contacted on telephone (03) 62305426 or by E-mail: [peter.rayner@oa.hydro.com.au](mailto:peter.rayner@oa.hydro.com.au)

Yours faithfully,

Gary Baker  
Chief Executive Officer

Submission by the Hydro-Electric Corporation to the  
House of Representatives Standing Committee on Environment, Recreation and the Arts  
*Inquiry into the Regulatory Arrangements for Trading in Greenhouse Gas Emissions*

## **INTRODUCTION AND SUMMARY**

Tasmania's Hydro-Electric Corporation (HEC) recognises the global problems arising from continued emission of air pollutants which are generally associated with a number of major sources and industries, including the electricity generation sector.

HEC endorses the greenhouse gas (GHG) emissions trading component of the Kyoto Protocol as a realistic mechanism to assist in the reduction of air pollutants and commends the Federal Government's initiative to pursue a domestic framework to support the international protocol.

HEC appreciates that the Federal Government's responsibility is to establish an emissions trading framework that will facilitate the reduction of GHG emissions from all significant sources while balancing the costs of those reductions against the overall economic impact on the country. It is understood that the electricity sector is a key element and that initial effort may well be concentrated on this sector.

As perhaps the longest standing large scale electricity generator in Australia, the HEC has a history linked almost exclusively to clean, renewable electricity production but recognises that the bulk of the country's electricity needs are met from fossil fuel sources and that this situation will continue well into the future.

The HEC urges the Government to initiate an emissions trading framework which:

- will result in the rapid development of an emissions trading market;
- will integrate with other GHG reduction strategies;
- will not further disadvantage non-polluting generators to the benefit of fossil fuel generators;

To achieve this, the **HEC recommends the Government use a "grandfather" approach to allocate emissions credits to the whole of the electricity sector based on units of output (eg GWh per annum or MW of installed capacity).**

The HEC does **not support** either a **full auction** of emissions credits **or a grandfather allocation based solely on a generator's emission history.**

## **REDUCTION STRATEGIES**

In the electricity industry, greenhouse gases can be reduced by:

- a) cutting the consumption of fossil fuels;
- b) encouraging the use of renewable non-polluting energy sources (eg hydro, wind);
- c) becoming more energy efficient;
- d) adopting measures that enhance carbon sequestration.

HEC is well placed to make positive contributions to Australia's overall GHG reduction effort particularly through (b) and (c) above. But in order to be a contributor, HEC, together with all other non-polluting generators, must not be disadvantaged by an emissions trading framework that gives potential benefits and financial incentives only to those generators which have a history of polluting.

#### **EMISSIONS TRADING FRAMEWORK BASIS**

The framework which the Government wishes to establish to facilitate domestic emissions trading should be based on the following fundamentals:

- accountability at the point where emissions occur or would occur if preventative action were not taken;
- a trading system which is market driven rather than a regulatory imposition;
- a market which is dynamic from the outset, ie does not have to wait for participants to improve their emissions performance to have tradeable stock;
- a level trading field reflecting the market's determination of the true, or whole, cost of electricity. [Clean generators are already financially disadvantaged since their transparent full cost of generating has to compete with the "artificially discounted" cost of fossil fuel energy which has not had the large environmental impact cost factored in.]

Cleaner, or non-emitting, generators would be valuable participants in an emissions trading market and would provide a vital early stimulus to the market, provided they have access to emissions credits at an early stage.

#### **ALLOCATION OF EMISSION CREDITS (THE RIGHT TO EMIT GREENHOUSE GASES)**

An emissions trading system is likely to be based on the trade of emissions credits which will be initially allocated by the Government. HEC views the mechanism for allocation of credits as a key issue and one which could lead to inequities and financial disadvantage if inappropriately formulated.

A full auction could be implemented to allocate emissions credits but this approach is not favoured by the HEC for the following reasons:

- it would impose an additional financial burden on non-polluting generators wishing to become entrants in the emissions trading system;
- the credit purchase costs are likely to be passed on in some form to the detriment of the Australian economy as a whole.

A "grandfather" approach would minimise overall detrimental economic impact, but the allocations would need to be implemented to a formula which would be non-discriminatory and which would stimulate early market trading.

Grandfather allocations made solely on the basis of a generator's emissions history would discriminate against clean generators (nil or few credits because of good performance) and would exacerbate the distortion of the true cost of fossil fuel generation by providing a non-costed allowance. In addition, credits may not be available for trading until the generator improved its emissions output, thus delaying the development of a dynamic market.

The HEC believes that grandfather allocations made to all participants in the industry based on units of output (eg GWh per annum or MW of installed capacity) would be a more equitable formula. While still resulting in the bulk of allocated credits going to the fossil fuel generators to stimulate GHG improvement, this approach would:

- enable clean generators to participate on an equal basis to thermal generators;
- result in credits being available for immediate trading;
- enhance competition between clean and polluting generators;
- encourage investment and growth by clean or renewable generators;
- facilitate developments to meet the Government's mandated renewables target;
- enable the market to determine the true cost of generation.

There has been some discussion on the concept of cleaner generators being allowed a percentage increase in emissions as a way of giving them entry into an emissions trading market. This would not be a feasible strategy for a zero emitter such as a hydro generator, since 120% of zero is still zero!

### **EMISSION OFFSETS**

HEC strongly supports the concept of emission offsets, ie compensating for increased emissions from one source by reducing emissions from another.

The proposed Basslink power cable linking the HEC's clean, renewable energy source with mainland Australia's predominantly fossil fuel system will provide a mechanism for effectively implementing emission offsets through:

- a) power purchases - enabling mainland industrial customers with GHG emissions to purchase clean electricity as an alternative to fossil fuel energy;
- b) power exports - enabling HEC to export clean electricity as a displacement for mainland thermal generation, particularly in times of peak demand or when HEC would be spilling water from dams to waste during periods of high rainfall;
- c) development of renewables - providing a commercial customer base to enable Tasmania to pursue the development of its other natural renewable energy sources such as wind and biomass.

[All of these would also facilitate the Government's mandated renewables policy]

These emission offsets based on a Basslink connection would be dependent on Tasmania's clean renewable energy production not being financially disadvantaged by an inappropriate emissions trading mechanism.

### **RECOMMENDATION**

The HEC recommends to the Committee that in the allocation of the right to emit greenhouse gases (Terms of Reference point 3), initial allocations by Government be a **“grandfather” approach to the whole of the electricity sector based on units of output (eg GWh per annum or MW of installed capacity).**

### **SIGNED**

Gary Baker

Chief Executive Officer  
6 July 1998