

## **Submissions on the proposed Clean Energy Legislative Package**

### **A. Introduction**

1. On 28 July 2011, the Australian Federal Government (“the Government”) introduced its Clean Energy Legislative Package<sup>1</sup> (“the Package”) designed to reduce carbon emissions and support its policy in relation to climate change. The primary legislative instrument within the Package is the *Clean Energy Bill 2011* (“the Bill”).
2. The main objectives of the Bill are to give effect to Australia’s obligations under the Climate Change Convention and Kyoto Protocol, support the development of an effective global response to climate change and significantly reduce Australia’s net greenhouse gas emissions by 2050.<sup>2</sup>
3. In order to facilitate these objectives, the Government is to introduce a carbon emissions cap for greenhouse gas emissions and a carbon pricing mechanism under the Bill.
4. Under the carbon pricing mechanism, Australia’s biggest polluters (so-called “liable entities”), being those entities that emit greenhouse gases with a carbon dioxide equivalence in excess of 25,000 tonnes per financial year, must pay for each tonne of greenhouse gas emissions they release into the atmosphere.<sup>3</sup>
5. The intended effect of the carbon pricing mechanism is to create incentive for industry to reduce their greenhouse gas emissions by operating more efficiently and investing in cleaner technologies.
6. ATCO Gas Australia Pty Ltd (“ATCO”) is a major participant in the energy sector of Western Australia, with its gas distribution system (“GDS”) being the major distribution pipeline network for natural gas in the State. ATCO’s GDS comprises approximately 12,800 km of pipeline and provides gas

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<sup>1</sup> The *Clean Energy Bill 2011*; The *Clean Energy Regulator Bill 2011*; The *Clean Energy (Consequential Amendment) Bill 2011*; and The *Climate Change Authority Bill 2011*; *Clean Energy (Unit Shortfall Charge-General) Bill 2011*; *Clean Energy (Unit Issue Charge-General) Bill 2011*; *Clean Energy (Charges -Excise) Bill 2011*; *Clean Energy (International Unit Surrender Charge) Bill 2011*; *Ozone Protection and Synthetic Greenhouse Gas (Import Levy) Amendment Bill 2011*; *Ozone Protection and Synthetic Greenhouse Gas (Manufacture Levy) Amendment Bill 2011*; *Excise Tariff Legislation Amendment (Clean Energy) Bill 2011*; *Customs Tariff Amendment (Clean Energy) Bill 2011*; *Fuel Tax Legislation Amendment (Clean Energy) Bill 2011*; and presently a Bill is being drafted in relation to households: *Clean Energy (Household Assistance) Amendment Bill 2011*.

<sup>2</sup> Section 3 of the Bill.

<sup>3</sup> Sections 4 and 20(4)(b) of the Bill.

distribution connection to nearly 650,000 end use points, serving over 1,700,000 Australians.

## **B. Australia's Energy Sector**

7. Electricity generation is Australia's largest source of greenhouse gas emissions, being responsible for just over a third of Australia's total greenhouse gas emissions.<sup>4</sup>
8. More specifically, coal-fired electricity generation complexes are amongst the largest emitters of greenhouse gas.<sup>5</sup>
9. Natural gas, however, produces less than half the greenhouse gas emissions of coal, and as such, represents a highly efficient and low environmental cost/impact fuel in the production of electricity.<sup>6</sup>
10. Combined cycle gas-fired generation and co-generation plants are recognised as leading edge, technologically advanced, reliable and environmentally low-impact forms of non-renewable power generation.<sup>7</sup>
11. A natural gas combined cycle plant produces less than half the level of greenhouse gas emissions compared to an equivalent capacity coal-fired power plant for every megawatt per hour of electricity generated.<sup>8</sup>
12. Given the high levels of greenhouse gas emissions generated, and inefficiency with which coal-fired electricity generation complexes produce electricity, the Government has acknowledged that the transition to a carbon price will have significant and costly implications for the coal-fired electricity generation sector.<sup>9</sup>
13. Specifically, the Government has acknowledged that (irrespective of the fact that coal-fired electricity generation complexes are able to pass-through the cost of the carbon pricing mechanism to customers), highly emissions-intensive coal-fired electricity generation complexes are likely to face an

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<sup>4</sup> Page 10 of the *Exposure Draft of the Clean Energy Bill 2011 Commentary on Provisions* dated 28 July 2011.

<sup>5</sup> *Ibid* 4.

<sup>6</sup> p 52,53 of "State of the Energy Market 2009", Australian Energy Regulator ("AER") dated December 2009.

<sup>7</sup> Research Note 21 1998-99 "Cogeneration-Combined Heat and Power (Electricity) Generation", Michael Roarty, Science, Technology, Environment and Resources Group (Parliamentary Library).

<sup>8</sup> Note 6 above

<sup>9</sup> Page 146 of the *Exposure Draft of the Clean Energy Bill 2011 Commentary on Provisions* dated 28 July 2011.

increase in their operating costs greater than the general increase in the level of electricity prices passed onto customers.<sup>10</sup>

14. In order to assist highly emissions-intensive coal-fired electricity generation complexes to remain competitive with other less emissions-intensive generation complexes and transition to a carbon price, the Government has made provision under the Bill for the allocation of free carbon units to coal-fired electricity generation complexes that meet certain criteria (“eligible generation complexes”) and other financial assistance (in terms of cash payments).
15. No such provision is made in relation to the natural gas sector.
16. The rationale for the allocation of free carbon units to eligible generation complexes is, *inter alia*, to maintain energy security and support investor confidence in the coal-fired electricity generation sector.

### **C. Impact of the Bill on the Natural Gas Sector**

17. The price competitiveness of natural gas compared to coal in Western Australia has been declining due to a combination of factors including comparative production costs and the structure and operation of the Western Australian domestic energy market<sup>11</sup>.
18. The carbon pricing mechanism will have significant and costly implications for the natural gas sector, which is likely to adversely impact on its price competitiveness.
19. In the event that the coal-fired electricity generation sector receives “assistance” from the Government under the Bill (through the allocation of free carbon units and other cash payments), there are likely to be several unintended consequences, including a further negative impact on the natural gas sector’s price competitiveness but also **increased** overall emissions.

#### **a. Price Competitiveness**

- i. As noted above, the allocation of free carbon units to eligible generation complexes is intended to allow them to remain competitive with other less

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<sup>10</sup> Ibid 9.

<sup>11</sup> See analysis in “Inquiry into Domestic Gas Prices” Report, Economics and Industry Standing Committee, Parliament of Western Australia, 23 March 2011.

emissions-intensive generation complexes and to allow a smooth transition to a carbon price. That is, the Government's assistance is aimed at assisting eligible generation complexes to remain competitive within *their own energy sector* and somewhat relieve the financial pressure experienced as a result of the carbon pricing mechanism.

In circumstances where other energy sectors, including the natural gas sector, are not afforded the same, or similar, assistance under the Bill, their businesses will be significantly impacted in terms of the costs imposed by the carbon pricing mechanism. Moreover, an unintended consequence of the Government's assistance to eligible generation complexes is that *other energy sectors*, including the natural gas sector, are likely to be negatively impacted in terms of their price competitiveness. That is, by providing assistance to the coal-fired electricity generation sector such that the price of electricity is likely to remain stable, the natural gas sector (which will have to pass-through the effect of the carbon pricing mechanism to consumers) is likely to become less price competitive than the coal-fired electricity generation sector.

- ii. Although the assistance which is to be provided to eligible generation complexes is likely to encourage moves to less emissions-intensive electricity generation in the longer term (including gas-powered generation), in the short to medium term, the assistance will ensure that coal-fired electricity generation complexes will continue to remain a less expensive source of energy for customers. Again, in these circumstances, the unintended consequence of the Bill is that the natural gas sector may become less price competitive than its coal-fired electricity generation sector counterpart.
- iii. Another potential unintended consequence of the Government's assistance to eligible generation complexes is that electricity prices will remain less cost-reflective (subsidised in real terms) in comparison to natural gas. This may act as a disincentive for customers to choose more efficient gas heating and cooking appliances over less efficient and, higher emitting, electrical appliances when the efficiencies and make-up of electricity generation, transmission and distribution are fully considered;
- iv. A further potential unintended consequence of the emissions intensity and trade exposure ("EITE") provisions of the Bill is the incentive to gas

producers to choose to export natural gas as LNG (and qualify for the EITE supplementary allocation of permits), and a disincentive to supply the domestic gas markets in Australia.

If gas producers incur carbon price regime costs and are unable to pass those costs on to customers, producers face a further incentive to choose to export natural gas over domestic gas market supply.

If gas producers are able to pass on the carbon price regime costs to customers, domestic market natural gas prices will increase, and further widen the cost gap between electricity and natural gas an energy source of choice for consumers.

It is also possible that producers may curtail or defer planned Australian gas exploration, development and production projects in preference to opportunities in other parts of the region placing further domestic market supply restrictions and upward pressure on natural gas prices.

- v. Finally, the likely imbalance in the price competitiveness of the natural gas sector compared to coal-fired electricity generation sector (as a consequence of the Government's assistance to eligible generation complexes) in the circumstances outlined above, may result in reduced energy security and investor confidence in the natural gas sector, and have the detrimental consequence of fundamentally disadvantaging Australian households.

**b. Objectives of the Bill**

The stated objective of the Bill is, *inter alia*, to act as an incentive for high emitters to reduce their greenhouse gas emissions. This objective is achieved by effectively penalising high emitters by imposing a cost consequence (via the carbon pricing mechanism) on pollution.

Irrespective of the stated objective, the unintended consequence of the Bill as currently drafted, is to effectively reward high emitters in the coal-fired electricity generation sector through the provision of financial support to offset the effect of the carbon pricing mechanism and free up funds for investment in cleaner technologies to further reduce any exposure under the carbon pricing mechanism in the future.

In contrast, cleaner energy producers in the natural gas sector are penalised by not only being exposed to the costs under the carbon pricing mechanism, but also the cost of investing in cleaner technologies to further reduce their costs exposure under the mechanism.

#### **D. Submissions**

20. For the aforementioned reasons, it is submitted that the Government should make provision under the Bill to provide the same level of assistance to the natural gas sector as provided to the coal-fired electricity generation sector.
21. In so doing, it will ensure a more *“level playing field”* between the natural gas sector and the coal-fired electricity generation sector in terms of price competitiveness and promote energy security and investor confidence in the natural gas sector, as well as, make more funds available within the sector to invest in cleaner technologies for the ultimate benefit of Australian households.
22. It will also ensure that the natural gas sector within Western Australia (which supplies approximately 55.0% of Western Australia’s primary energy requirements)<sup>12</sup> will not deteriorate any further.

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<sup>12</sup> “Energy in Australia 2010” (Energy Consumption, 2007-2008), ABARE