



30 May 2013

Anthea Harris
Chief Executive Officer
Climate Change Authority
GPO Box 1994
Melbourne VIC 3001

Lodged via www.climatechangeauthority.com.au

Dear Ms Harris,

Caps and Target Review, Issues Paper

Alinta Energy welcomes the opportunity to make a submission in response to the Authority's *Caps and Targets Review*, issues paper.

Alinta Energy is an active investor in the energy retail, wholesale and generation markets across Australia. Alinta Energy has over 2500MW of generation facilities in Australia (and New Zealand), and a growing customer base of approximately 700,000 retail energy customers.

Alinta Energy acknowledges that the Caps and Target settings will inform Australia's national emission trajectory, timeframe, budget and environmental and emission reduction objectives.

Alinta Energy understands any recommendations provided by the Authority are produced with a mind to reducing uncertainty and providing a framework within which businesses and investors can make certain long term decisions.

Nevertheless, many of the Authority's assumptions are dependent on several critical variables that are unresolved, this includes the absence of domestic bipartisan support, the stability of the European Union emissions trading scheme, international linkage, and the role of a Australian carbon price.

In this regard, the avoidance of existing political, economic and policy uncertainties, both domestically and internationally, characterises much of the Authority's approach. Alinta Energy understands that the Authority is duty bound to progress the review; however, this makes responding to the review challenging.

Whilst Alinta Energy understands that many of these uncertainties sit outside the Authority's mandate, it is preferable that the Authority ensure any recommendations take into account highly likely, if not market accepted outcomes. Recommendations by the Authority which disregard these considerations will inevitably be misplaced.

The inclusion of such considerations would also address stakeholder uncertainty, as well as ensuring an appropriate balance between environmental objectives and economic concerns. Alinta Energy's submission should be examined within this context.

Australia's 2020 Target

Alinta Energy understands the environmental objectives endorsed by the Government, including Australia's goal of limiting global temperature rises to less than two degrees.

Alinta Energy appreciates that the setting of a global emissions budget illustrates where different national budgets and targets would need to remain in order to meet a global emissions target. As such, it is clear that any target for Australia by 2020 should not be considered without reference to international developments.

Alinta Energy considers the current Cancun agreement framework with which Australia's commitment is assessed is a suitable structure from which to benchmark Australia's 2020 obligations.

Under the Cancun agreement Australia does have the opportunity to expand its commitment to 15% emissions reductions by 2020, if other advanced economies achieve "*substantially measurable, reportable and verifiable commitments and actions*".

Nevertheless, present international developments (outlined below) make it clear that both the policy settings and the science related aspects of global emissions reductions are not static. This actuality is reflected in the Authority's own view on the flexibility of Australia's target.

On this basis, absent significant international progress, there is no case which warrants Australia increasing its emission reduction target beyond the 5% currently committed. Doing so would potentially lock Australia into costly obligatory policy settings, which will be immaterial in achieving the original global objective.

How Australian action can influence international emission reductions

Alinta Energy notes the Authority's view that "*an effective solution to climate change requires action by at least all the major emitting economies*".² To this extent, Australia is only a component part of a possible global solution.

Whilst not commentating on the appropriateness of actions to date, it is clear Australia undoubtedly has shown singular commitment. This includes implementing a carbon tax, setting a ambitious Renewable Energy Target, constructing a government funded Clean Energy Finance Corporation as well as the formation of various other national green schemes and energy efficiency programs.

Nonetheless, Alinta Energy understands that a view exists that Australia has a limited ability to influence other nations in regards to the setting of targets. Several recent international developments validate this view including the fact that:

- the 2009 Copenhagen and 2011 Durban conferences were both characterised by deadlock and lack of consensus;
- in 2011 Canada removed itself from the Kyoto Protocol;
- the United States of America is effectively reducing its emissions without any formal agreement;
- there are a number of questions about the survival of the European Union Emission Trading Scheme;
- various developing major emitting countries still do not have the capability to accurately measure emissions, making it hard to measure and benchmark global progress; and

¹ "Australia's Emissions Reduction Targets", Department of Climate Change and Energy Efficiency.

² "Caps and Target Review" (2013), Climate Change Authority, Issues Paper, Pg 24

- many countries emission reduction targets are still non-binding and only set as ranges with no penalties for non-compliance.

On this basis, even given Australia's climate leadership aspirations, it is apparent that due to Australia's relative size in the context of global emissions, there is a limited ability for Australia to meaningfully influence global abatement levels and international debate regarding this issue.

As such, Alinta Energy suggests the authority concentrate on policy outcomes which are linked to collective levels of verifiable international progress.

Timeframes

Alinta Energy understands the Authority is tasked with recommending an appropriate timeframe period in which Australia's accepted emission reduction targets can be suitably assessed, with the intention of informing the marketplace and reducing uncertainty.

However, there exist significant challenges in providing long term guidance on the scale and rate of Australia's emission reductions beyond 2020. Alinta Energy notes that whilst attempts at such forecasts will no doubt be of interest, they are in the context of international developments inconclusive.

The United States of America's present domestic natural gas boom, which has led to an unforeseen rapid decline in carbon emissions to 1994 levels is a telling example³. Gas fired generation is now displacing coal at such a rate that the United States is now curbing emissions faster than Europe. This unpredicted reduction in emissions is all the more notable because of the limited role of government energy regulations and policies.

As such, there is little reason to expect Australian forecasts will bear reasonable resemblance to actual outcomes. This is amplified given the noted policy uncertainties. Therefore, any range of forecast trajectories may be of value as a guide but not for the purpose of determining actual obligations.

Accounting

Alinta Energy agrees with the Authority's view that in setting a target, trajectories and budgets must report which exact emissions count towards individual targets. Australia's commitment to the Kyoto Protocol accounting procedures currently set the benchmark in which to measure progress.

Australia has exerted significant economic effort in this regard, at considerable cost, and has achieved a noteworthy overall reduction in emissions, achieving a 105 per cent level of 1990 emissions, well below the 108 per cent target level set.

The current "carry over" accounting settings are a well designed insurance provision which allows Australia to use its surplus reductions to manage any higher emissions in future periods. This principle is entirely appropriate as it provides flexibility as new economic challenges surface.

It seems overly ambitious and counterproductive to exclude the emission reductions Australia has achieved above and beyond the current Kyoto obligations. Openly canvassing options of strengthening Australia's emission reduction goals by cancelling surplus units would render the entire rationale for establishing a benchmark from which to measure progress redundant.

Alinta Energy does not support any accounting measure to voluntarily cancel units which Australia has worked hard to achieve. Any attempts at doing so are ill-advised and can only undermine the value of current regulations.

³ "Why the US is Cutting Carbon Faster than Europe" (April 2013), Bloomberg Business Week – Global Economics.

Caps

Given the reduced clarity surrounding Australia's present limits on importation of permits, a fixed carbon price, and global uncertainty on emissions estimates, Alinta Energy would caution against setting an inflexible annual emission cap.

Alinta Energy suggests the Authority should consider annual emissions caps which follow the trajectory on a flexible year by year basis; accounting for the significant uncertainty which exists. In general this means caps being set looser in initial years, which provides short-term liquidity and allows the market to adjust for tighter future years.

Alinta Energy considers this approach would be consistent with the national budget and trajectory.

The Economic and Social Implications of Different Emissions Reduction Goals for Australia

Issues of global free riding

Alinta Energy notes the Authority's view that achieving global emission reductions is in Australia's national interest. This principle is reflected in actions taken to date; however, in practise assessing the burden each member nation undertakes is significantly difficult.

Alinta Energy understands that the issue of free riding is an emerging concern from various stakeholders, and is a substantial issue yet to be comprehensively addressed by the Authority.

Arguments around Australia taking the lead in rapid and deep emission reductions fail to address the inherently all-inclusive nature of global warming expectations. Australia setting ambitious policy objectives in the absence of measurable global action, whilst well intentioned, may encourage other nations to "free ride" on Australia's efforts in reducing global emissions.

Free riding nations can effectively engage in strategic behaviour by undertaking only modest emission reductions whilst gaining benefits through other countries more significant reductions.

This happens when individual nations incur a "leadership premium" and reduce their emissions in the absence of global consensus, which incentivises other nations to effectively undercut collective action and "free ride" on these emission reductions. This puts those countries incurring the "leadership premium" at an economic disadvantage.

On this basis, options to further enlarge Australia's ambitious leadership cannot be assessed in the absence of a comprehensive examination of the "free rider" effects.

Modelling of costs

The Authority's work is directed by the principles as set out in the *Clean Energy Act 2011* and the *Climate Change Authority Act 2011* which guides the Authority's recommendations in regards to being "economically efficient, environmentally effective, equitable and in the public interest".

Alinta Energy is encouraged that the Authority has accurately identified the need for substantial economic modelling of the impact of the significant cost burden placed on Australian households through higher energy prices.

Alinta Energy considers modelling should be extended to consider the additional cost of incurring a "leadership premium". Whilst the benefits of being a global leader in promoting global climate change policies are enthusiastically and widely promoted, the corresponding costs are often overlooked.

Given Australia's social legacy, political and economic justifications remain largely unresolved in relation to this issue; it is clear that the "leadership premium" is a principle which warrants detailed evaluation.

Conclusion

Alinta Energy suggests that in the pursuit of broad public policy goals, that a credible starting point is as important as the intended policy outcome. On this basis, Alinta Energy welcomes the Authority's analysis and encourages further consideration of the matters enunciated above in the context of the current political and economic environment.

Should you have any queries in relation to Alinta Energy submission, or wish to discuss these matters more generally, please do not hesitate to contact me on, telephone, 02 9372 2633, or Anders Sangkuhl on, telephone, (02) 9375 0962.

Yours sincerely,



Jamie Lowe
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