Business Council of Australia

Submission on

Renewable Energy Target and Treatment of Electricity-Intensive, Trade-Exposed Industries

to the

Renewable Electricity Markets Team

and the

Renewable Energy Sub Group Secretariat
Renewables, Offsets and COAG Branch

Department of Climate Change

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EXECUTIVE SUMMARY

The BCA's vision is for Australia to be the best place in the world in which to live, learn, work and do business and for it to become and remain a top-five economy among OECD countries by 2012. The overriding objective is to enhance prosperity in Australia.

The BCA makes this submission giving consideration to Australia's long-term economic prosperity, as it is the strength of Australia's economy and viability of Australia's businesses that will ensure we are able to respond to economic, social and environmental challenges, including climate change.

The proposal to expand the government's renewable energy target is occurring at a time of a sudden and severe downturn in the global economy, which in turn has brought significant uncertainty about Australia's short-term economic outlook, with likely flow-on concerns, for example due to the terms of trade impact over the medium term.

The BCA has considered the proposed implementation of the expanded renewable energy target in a number of earlier submissions to government.

In these submissions the BCA has highlighted that the proposed expanded renewable energy target fails to meet the tests the government has prescribed for the introduction of policies that are complementary to the Carbon Pollution Reduction Scheme (CPRS). In particular, the proposed expansion of the renewable energy target is occurring without the evidence of market failure, and does not ensure least-cost emission reduction.

The release of the COAG Principles for the Jurisdictions to Review and Streamline their Existing Climate Change Mitigation Measures in November 2008 has further reinforced the commitment of state and federal governments to these tests.

The BCA submissions have also highlighted that an expanded renewable energy target will lead to higher-cost emissions abatement.

This matter has been further addressed in the Treasury modelling released in October 2008, titled `*Australia's Low Pollution Future: The Economics of Climate Change Mitigation*, which points out that the cost of emissions reductions through the introduction of the renewable energy target will be up to three times higher than the cost of permits under the CPRS for the period 2010 to 2020. Such an analysis points to the fundamental conflict between the stated aim of the CPRS to facilitate least-cost emissions reduction, and the introduction of an expanded renewable energy target which leads to additional costs to achieve emissions reduction.

Given the expanded renewable energy target does not meet the criteria for a policy that is complementary to the CPRS and will lead to additional costs to achieve emissions reduction, it would be appropriate for the government to reconsider the policy objective it wishes to achieve and whether there are other more appropriate policy tools to bring forward both renewable and low-emissions technologies without undermining the CPRS. Such policies could include targeted research, development and deployment initiatives to address specific challenges in technology development.

If such a reconsideration of the proposed policy is not to be undertaken, the proposed renewable energy target draft legislation and related treatment of electricity-intensive, trade-exposed industries (RATE industries) require careful consideration.

An overarching consideration is the methodology being used to estimate the 20 per cent target in gigawatt hours in 2020. There is a substantial difference in the energy demand estimates used in the draft legislation and the CPRS white paper, with the draft legislation estimate of 45,000 gigawatt hours being some 8,000 gigawatt hours higher than that in the white paper. It is unclear why the draft legislation is prescribing a higher figure. In drafting the legislation this potential confusion needs to be rectified and the basis for any quantity measures made transparent.

A number of other drafting issues are referred to later in this submission.

Equally as important will be ensuring the expansion of the RET includes provisions to address the possible impacts on trade-exposed industries using electricity. In essence, all trade-exposed industries (using the definition in the CPRS) should be fully exempted from the impact of the RET.

While it has been suggested that the CPRS activity test could be the starting point for such an approach, this is not feasible given the ongoing consultation required to work through the details such as activity definition.

At a minimum, should the RET proceed, the approach will need to be equivalent to that which has been taken in both the Victorian and New South Wales state schemes, that is, the amount of electricity consumed by electricity-intensive, trade-exposed industry should be netted out from total electricity consumption and excluded from the assessment of parties liable to meet the annual RET targets. Such an approach will assist in managing the impact and not lead to an increased burden on other businesses, other than that related to the price impact.

INTRODUCTION

The Business Council of Australia (BCA) represents the chief executives of over 100 of Australia's leading companies. The BCA develops and advocates, on behalf of its members, public policy reform that positions Australia as a strong and vibrant economy and society. The businesses that the BCA members represent are among Australia's largest employers and represent a substantial share of Australia's domestic and export activity. Therefore they have a significant interest in the scope and direction of economic reform.

The BCA's vision is for Australia to be the best place in the world in which to live, learn, work and do business and for it to become and remain a top-five economy among OECD countries by 2012. The overriding objective is to enhance prosperity in Australia.

Such an objective is not at odds with effective environmental management, but does require reforms aimed at 'internalising' environmental costs and risks, most notably with regard to greenhouse gas emissions and the risks associated with climate change.

The response should be based in a suite of policies that are complementary and facilitate least-cost abatement. It also requires the introduction of such policies in a manner that does not disadvantage Australia's competitiveness or put employment at risk, but rather, in a manner that ensures a smooth long-term transition to a low-emissions economy.

This submission reiterates the concerns raised by the BCA previously with regard to the introduction of an expanded renewable energy target (RET) and more significantly addresses the need to ensure the competitiveness of the electricity-intensive, trade-exposed industries should not be disadvantaged by the introduction of the RET.

COMMENTARY ON THE PROPOSED EXPANSION OF THE RENEWABLE ENERGY TARGET

With the election of the current federal government there is a renewed focus on national and international responses to climate change and in particular the design of a national emissions trading scheme.

The federal government has simultaneously announced the implementation of a renewable energy target (RET) with an expected starting date in mid-2009, a review in 2015 and phasing out between 2020–2030 and the establishment of the carbon pollution reduction scheme (CPRS) with trading commencing in 2010.

The key challenge in considering the RET policy is whether it will ensure Australia can achieve its emissions reduction in the most cost-effective way and that the introduction of this policy does not lead to adverse impacts on Australia's internationally competitive, electricity-intensive industries.

The implementation of the Australian emissions trading scheme should be the primary vehicle to achieve emissions reduction.

Additional policies and programs should only be introduced to address a specific market failure not addressed through the emissions trading scheme.

The release of the 'Principles for the Jurisdictions to Review and Streamline their Existing Climate Change Mitigation Measures' by the Council of Australian Governments in November 2008 makes clear the tests any complementary policy should clear before it is implemented, that is, it is targeted at a market failure that is not expected to be adequately addressed by the Carbon Pollution Reduction Scheme or targeted to manage the impacts of the Carbon Pollution Reduction Scheme on particular sectors of the economy.

An assessment of the RET in light of these principles would suggest the RET policy should not be proceeded with.

The BCA submissions have also highlighted that an expanded renewable energy target will lead to higher-cost emissions abatement.

This matter has been further addressed in the Treasury modelling released in October 2008, titled *Australia's Low Pollution Future: The Economics of Climate Change Mitigation*, which points out that the cost of emissions reductions through the introduction of the RET will be up to three times higher than the cost of permits under the CPRS for the period 2010 to 2020.

Such an analysis points to the fundamental conflict between the stated aim of the CPRS to facilitate least cost emissions reduction and the introduction of an expanded renewable energy target which leads to additional costs to achieve emissions reduction.

This means Australian businesses will now face an additional cost over that arising from the CPRS at a time of a worsening economic outlook both in terms of the depth of the economic decline and its likely duration.

The global economy has deteriorated rapidly and sharply, even compared with expectations in late 2008. Global growth is now projected by the IMF to be 2.2 per cent in 2009, compared with 3¾ per cent in 2008 and 5 per cent in 2007.

The United States, Japan, the United Kingdom and European Union are in recession. The economies of China and India are slowing.[1] This suggests that further downward revisions in economic forecasts around the world are likely.

Recent data suggests Australia faces weak consumer spending and business investment growth and a substantial drop in demand for its exports. Where just a year ago excessive demand was exposing Australia's supply constraints, we now find economic demand needs support.

[1] Between October and November 2008, the IMF revised downwards its 2009 forecasts for growth in China from 9.3 per cent to 8.5 per cent and for India from 6.9 per cent to 6.3 per cent. The OECD has warned of a 'strong slowdown' in China (OECD, 'Composite Leading Indicators Signal Deep Slowdown in OECD Area and Major Non-OECD Member Economies', news release, 12 January 2009, Paris) The World Economic Forum says that decline in demand for China's exports is 'increasing considerably' the risk of a 'hard landing' (World Economic Forum, *Global Risks 2009* report, January 2009).

Rising capital costs and pressure on cash flows are now significant issues across business and will impact the capacity of business to manage the impacts of both the RET and the CPRS.

Whilst the RET may stimulate the development of renewable energy sources it remains unclear whether this will be done in the most economically efficient manner and whether it will bias the options for renewable energy expansion in a narrow manner.

ELECTRICITY-INTENSIVE, TRADE-EXPOSED INDUSTRIES

The introduction of the RET will bring with it additional costs for those industries using electricity as a means of production. Where industries cannot pass this cost on there is a change in the competitiveness of these industries relative to exports and imports.

It is essential that the introduction of the RET includes measures to offset this competitiveness impact from its commencement. In essence, all trade-exposed industries (using the definition in the CPRS) should be fully exempted from the impact of the RET.

While it has been suggested that the CPRS activity test could be the starting point for such an approach, this is not feasible given the ongoing consultation required to work through the details such as activity definition.

At a minimum, should the RET proceed, the approach will need to be equivalent to that which has been taken in both the Victorian and New South Wales state schemes, that is, the amount of electricity consumed by electricity-intensive, trade-exposed industry should be netted out from total electricity consumption and excluded from the assessment of parties liable to meet the annual RET targets. Such an approach will assist in managing the impact and not lead to an increased burden on other businesses, other than that related to the price impact.

SPECIFIC COMMENTS ON RENEWABLE ENERGY (ELECTRICITY) AMENDMENT BILL 2008

In considering the exposure draft of the Amendment Bill, the following comments are also made:

- At the core of the proposed amendment is the quantum of renewable energy required to meet the 20 per cent target in 2020. The draft legislation highlights a key concern as to how the 20 per cent target is determined. There is a substantial difference in the energy demand estimates used in the draft legislation and the CPRS white paper, with the draft legislation estimate of 45,000 gigawatt hours being some 8,000 gigawatt hours higher than that in the white paper. It is unclear why the draft legislation is prescribing a higher figure. In drafting the legislation this potential confusion needs to be rectified and the basis for any quantity measures made transparent.

- The legislation should make clear the conclusion date of the RET and specify the terms of the five-yearly review. Ambiguity as to the terms of the review and duration of the RET will have negative impacts on investment decisions.

- The shortfall charge under the RET should not be indexed. A cap on price in this way is justifiable as follows:

  - As the ETS cost grows (after a soft start) the price required by renewable projects should decline.

  - No indexation would be consistent with a gradual phase-out of the scheme, that is, the shortfall would reduce in real terms over time.

  - Any extension of the charge will provide windfall profits to existing REC suppliers.

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