



Centre for Energy and
Environmental Markets

Submission on Repealing the Carbon Price

by

Iain MacGill, Jenny Riesz and Regina Betz

Centre for Energy and Environmental Markets
University of NSW

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*Corresponding author: A.Prof. Iain MacGill
Centre for Energy and Environmental Markets,
The University of New South Wales, Sydney, NSW2052, Australia.
Tel.: +61 411 042 502, Fax: +61 2 9385 5993.
E-mail: i.macgill@unsw.edu.au

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We would welcome comments and suggestions on this, and all CEEM publications. The corresponding author for this submission is A.Prof. Iain MacGill (email: i.macgill@unsw.edu.au)

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1 Introduction

This submission responds to the Consultation Paper on the repeal of the carbon price, released by the Australian Government Department of the Environment in October 2013,. The repeal of the current carbon pricing arrangements represents a very significant change to the broader climate and energy framework established by the previous Federal Government through its 'Clean Energy Future' package. As such, its removal needs to be considered in the broader context of this framework, and changes that are also being proposed to other key elements including the Clean Energy Finance Corporation.

In the absence of such consideration, there are risks of unintended consequences that adversely impact Australia's capability to coherently, comprehensively and, most importantly, effectively respond to our climate challenges.

As such, consultation regarding repeal of the current carbon price should ideally be done within a broader consultation process that includes the Federal Government's direction action plan.

The terms of reference for this consultation, therefore, appear unduly narrow, being limited to:

- identifying any technical issues with the draft carbon tax repeal bills; and
- identifying and managing transitional issues for liable businesses and other entities.

In our submission we address these, but also first take the opportunity to comment on the wider potential implications of this draft bill for an effective, efficient and equitable Australian response to climate change.

We would, of course, be happy and interested to discuss these comments further with the Government.

2 The climate change challenge facing Australia

As highlighted by recently released reports from the IPCC¹ and Climate Change Authority², the challenge for Australia is not to achieve a 5% reduction in climate change emissions from 2000 levels by 2020. Instead, it is to achieve emission reductions of the scale and speed required to fairly contribute to an effective global response. There has been bipartisan Australia support of a 2020 target of emission reductions between 5-25% depending on international progress.³

Just as important over the coming decade is establishing the technical knowhow, institutional capability and social consensus that will be required to achieve near

¹ IPCC (2013) *Fifth Assessment Report (Working Group 1 Summary for Policy Makers)*, www.ipcc.ch.

² CCA (2013) see www.climatechangeauthority.gov.au.

³ The Climate Institute, Media Briefing, October 2013.

complete decarbonisation of the Australian economy by 2050. The proposed repeal of the Australian carbon price needs to be considered in this regard.

Of course, it is not possible to actually repeal the current carbon costs being paid by Australia, and globally due to climate change. There are costs associated with mitigating climate change, and costs (the so-called social cost of carbon) associated with failing to do so. These social costs arise from the damage global warming is already causing to societal welfare, and the harms it seems likely to increasingly cause into the future. The existence of these potential costs are near universally acknowledged – as just one example the US government estimates a social cost of carbon as an input into the climate benefits and costs of government decision making. Their most recent estimate has a social carbon price of over A\$75/tCO₂e in 2020 given a 2.5% societal discount rate.⁴

The question, therefore, is not whether to pay a carbon price or not but, instead, who pays how much to whom to do what, when. There are certainly options to reduce emissions that don't explicitly place a specific price on carbon emissions. The Renewable Energy Target is just one example. There are many opportunities to cost effectively reduce emissions that aren't currently being properly exploited – energy efficiency is a key example. An appropriately structured, coherent and comprehensive series of direct interventions could certainly reduce emissions, and strengthen our capacity to reduce emissions further into the future. Having said that, the success of direction action approaches similar to those being proposed by the Government, including the former Coalition Federal Government's Greenhouse Gas Abatement Program (GGAP) and the previous NSW Government's Greenhouse Gas Abatement Program (GGAS), has been mixed.⁵

Nevertheless, it is difficult to see how Australia can effectively and efficiently achieve emissions reductions of the scale and speed required across the entire economy without placing some form of incentive and penalty on most of the key decision makers that will determine future emissions. This was intended to be the key role of the carbon price. There is a debate to be had about how effectively it was playing this role, however, it would be valuable to have the Federal Government better articulate how they plan to achieve comprehensive yet coherent action across the economy in its absence.

Another key aspect of the climate policy challenge is that of robustness. Given ongoing uncertainties in the climate science, it is entirely possible that the necessary scale and speed of emission reductions to avoid dangerous warming may be revised – up or down. Similarly, there is little clarity on what international consensus on mitigation may emerge over the next few years. Finally, there are inevitable uncertainties associated with particular policy measures themselves. Even the best designed policies may fail to achieve their desired ends. This is a particular issue with incentive based approaches that seek to change private sector decision making through financial carrots or sticks. It is inherently uncertain how these participants

⁴ US EPA (2013) <http://www.epa.gov/climatechange/EPAactivities/economics/scc.html>

⁵ See, for example, the review of GGAP undertaken by the Federal Auditor General (2010) *Audit Report No.26 2009–10 Performance Audit - Administration of Climate Change Program*. CEEM has undertaken extensive reviews of the NSW GGAS scheme over its life – more details are available at www.ceem.unsw.edu.au.

may choose to respond. As such, Australia's climate and energy policy framework will need to be robust against surprises – good or bad – on both the scale of the challenge and the best means of addressing it. Key elements of robust policy include the use of a portfolio of policies such that if one fails, others can continue to drive progress. Removal of the carbon price and associated institutional frameworks reduces the options available to the Government to drive action should circumstances change, or preferred approaches prove more challenging than expected.

With regard to the specific issues raised by the Government for this consultation we make the following comments.

3 Issues with the draft carbon tax repeal bills

We will not specifically comment on possible technical issues with the repeal bills. However, the complexity of the proposed changes and the number of bills that require modification highlights the detailed institutional and regulatory work that was required to establish the carbon price. These efforts have established a framework that may have considerable future value if circumstances change such that the Federal Government wishes to re-establish some form of carbon pricing.

We note that the Government intends to retain the National Greenhouse and Energy Reporting Act 2007 (NGER Act) and the Australian National Registry of Emissions Act 2011 (ANREU Act). This legislation plays a critical supporting role for abatement activities. We urge the Government to consider exploring further how existing institutional capabilities and frameworks can be retained, even if the carbon price is formally set to zero, in order to keep the widest range of options available for future policy efforts.

A particular case of this is the intention, as noted in the consultation paper, that the Climate Change Authority will be abolished. The Authority has a role beyond that of just the carbon price and appears to have developed valuable capabilities in policy assessment, as seen in their recent RET review, as well as leading discussion on issues of what national emission reduction target should be established. Authoritative, well informed and independent advice to Government on both policy assessment and targets is essential. If the Authority is to be abolished, has the Government yet established that the required capabilities are available within the Department of Environment?

4 Transitional issues for liable businesses and other entities.

The transitional challenges for parties currently liable under the carbon pricing arrangements, and broader stakeholders should not be under-estimated. Major policy change inherently creates uncertainty and repeal of the carbon price is certainly no exception.

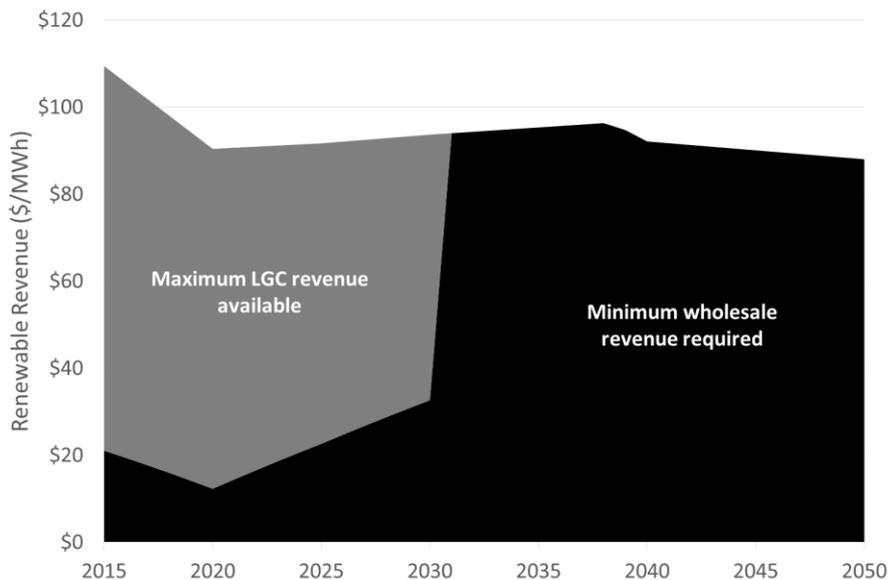
One concern that has been raised is that of potential windfall profits to liable entities who received free permit allocations under the so-called compensation arrangements of the Clean Energy Future package. It would be valuable for the Government to make public any analysis that it has undertaken on this vexed issue.

More generally, there are questions of transition for broader stakeholders in our energy and climate future that require consideration.

As noted earlier, a wide range of policies will be required to comprehensively address climate change, and transform the diverse sectors of Australia's economy towards low carbon alternatives. The carbon price was one pillar of the climate strategy of the previous Government. With the removal of the carbon price, it is therefore necessary to re-assess the remaining policy suite and ensure coherent and comprehensive coverage.

For example, analysis suggests that in the absence of the carbon price, the Renewable Energy Target (RET) will need to be strengthened in order to still achieve its legislated objectives. The RET and the carbon price were designed to work in partnership, with the price of Large-scale Generation Certificates (LGCs) rising and falling as necessary to hedge against movements in the wholesale electricity price (affected by the carbon price). With the removal of the carbon price, the wholesale electricity price can be expected to fall. This means that the LGC price will likely need to rise significantly to support continued investment in renewable generation.

The shortfall charge for the RET was set at a level that is appropriate in the presence of a meaningful carbon price. However, in the absence of a carbon price, it seems likely that the shortfall charge is too low to ensure continued investment in renewable generation. Figure 1 illustrates an estimate of the minimum wholesale electricity revenue required to promote continued renewable investment, based upon projected technology costs and the legislated shortfall charge. Based upon this analysis, with removal of the carbon price the RET shortfall charge will need to be increased significantly to ensure continued renewable investment. It would also seem appropriate that the shortfall charge is indexed at CPI to prevent decline in real terms. If the shortfall charge is not increased, retailers may prefer to pay the penalty fee rather than invest in renewable generation, causing increased costs to consumers without the positive outcomes of decarbonising the electricity sector, promoting rural development, and supporting the growth of the renewable energy industry.

Figure 1 - Minimum wholesale electricity revenue required to promote continued renewable investment

Source: Total renewable revenue required determined from levelised cost of least cost renewable technology in each year (wind and PV), sourced from Bureau of Resources and Energy Economics (BREE) Australian Energy Technology Assessment (AETA) 2012.

Furthermore, the RET ceases in 2030, which is already within the technical lifetime of renewable projects installed today. Retailers may well be reluctant to sign long term PPAs beyond the end of the RET unless there is confidence of electricity prices exceeding \$90/MWh. Given the intention of the present Government to repeal the carbon price this confidence is not likely to be forthcoming. In the absence of sufficiently long term PPAs (or confidence of sufficiently high LGC prices and electricity pool prices), renewable projects are likely to struggle to obtain financing. One way to address this issue would be to extend the RET beyond 2030, subject to a number of changes to the scheme including project sunsets, in addition to providing long term certainty on the scheme details, and an increase in the shortfall charge.

More generally, the Government should undertake a detailed and extensive review of the wide range of policies affecting the transition to a low carbon future to ensure comprehensive policy coverage, and policy coherence in the absence of the carbon price mechanism. Adjustments may be required in a range of these schemes to ensure continued effectiveness, and prevent unjustified cost burdens on consumers.

5 Acknowledgments

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