



**Energy Policy Institute of Australia**

**Second Submission to  
The Energy White Paper Process**

**The Institute's Detailed Comments and  
Submissions on the EWP 'Issues Paper'**

**4 February 2014**

## EXECUTIVE SUMMARY

Energy policy in Australia has been rendered irrelevant to investors; it is no longer either reliable or predictable. This is a matter of serious political, economic and social concern.

The principal explanation is an excessive level of politicisation of energy issues which has created policy uncertainty for investors.

Another explanation, unique to Australia, is that too many Parliaments are involved and there are limits to what can be achieved by 'cooperative federalism'.

In addition, the universal shortcomings of governments as efficient regulators of the modern energy industry have become apparent, as has the need to place greater trust in energy markets to allocate resources and deliver efficient outcomes.

Energy policy in Australia will remain irrelevant until it can be lifted to 'investment grade'. This cannot be achieved simply by calling for submissions and publishing an Energy White Paper - it will require a commitment to a three-stage process:

- First, Australia must adopt a long-term Australian energy vision – which should embody four key elements: (1) a resilient energy system, (2) export growth, (3) a low-carbon society and (4) innovation in energy production and supply.
- Second, agreement on the Australian energy vision should be arrived at by an apolitical, bipartisan process of stakeholder participation, involving industry, the community and all levels of government, a process that is not vulnerable to electoral cycles. This is the key to future policy reliability and predictability.
- Third, energy policy should be methodically, transparently and regularly reviewed over the long term, which requires an institutional mechanism to be established for the purpose.

The Institute has outlined 26 specific recommendations in this submission for consideration by the Australian government.

The Institute's recommendations will be debated at the Energy State of the Nation (ESON) forum to be held in Sydney on 21 March 2014.

## INTRODUCTION: THE NEED FOR A NATIONALLY AGREED ENERGY VISION

### *An integrated, coherent energy policy*

The Energy Policy Institute of Australia is an independent, apolitical, technology-neutral energy policy body. Since August 2009, the Institute has advocated:

*“In the interests of reducing policy uncertainty and of lowering the risk to investment in the energy industry, governments should no longer pursue energy policy and climate policy independently of each other – governments must integrate energy policy and climate policy into a coherent whole, whilst they continue to facilitate open energy markets.”<sup>1</sup>*

The Institute therefore very much welcomed the government’s choice of words on releasing the terms of reference on 5 December 2013 for the preparation of a new Energy White Paper (EWP):

*“The Australian Government is committed to working closely with industry and state and territory governments in the development of an integrated, coherent national energy policy.”*

This is of course easier said than done but we certainly agree that it must be done.

### *A nationally agreed energy vision*

On 9 December 2013, the Institute responded to the terms of reference with its first submission. The Institute emphasised the priority need for a nationally agreed energy vision.<sup>2</sup>

#### **Recommendation 1:**

***Australia’s central energy policy requirement must be a nationally agreed energy vision. This vision should embrace four policy goals:***

- (i) That Australia maintains a resilient energy system, providing all consumers with a reliable and affordable supply of energy and enabling the industry to function and prosper in a range of policy and economic scenarios;***
- (ii) That Australia grows its export earnings, providing a reliable and competitive supply of energy to its key customers around the world;***
- (iii) That Australia moves progressively towards a low-carbon society in tandem with its key trading partners without jeopardising its international competitiveness; and***
- (iv) That Australia becomes an innovative country, pursuing energy efficiency and energy innovation in collaboration with its trading partners and across an open and unobstructed portfolio of energy technologies.***

<sup>1</sup> Energy Policy Institute of Australia, “Energy Policy and Climate Policy Must Be Integrated”, August 2009 – [click here](#) or go to [www.energypolicyinstitute.com.au](http://www.energypolicyinstitute.com.au).

<sup>2</sup> Energy Policy Institute of Australia, “A National Energy Vision, A Safe Place to Invest and a Whole of Government Approach to Energy Policy Formulation,” 9 December 2013 – [click here](#) or go to [www.energypolicyinstitute.com.au](http://www.energypolicyinstitute.com.au).



In identifying affordability as one of the elements of a resilient energy system, the Institute emphasises that this is best achieved by the efficient operation of competitive energy markets.

We elaborate on how national agreement might be achieved in Part 2 of this submission.

On 17 December 2013, the government released an Issues Paper (the EWP Issues Paper) seeking comments to inform the government in the preparation of a future Green Paper, intended to be released in May 2014. This second submission by the Institute responds to the EWP Issues Paper. It is intended to complement its first submission and both should be read together.

### ***The excessive politicisation of energy issues and the resulting irrelevance of energy policy***

Australia has for some years lacked a reliable or 'investment grade' energy policy. The Institute outlined its reasons for this in its December 2012 commentary on the former government's EWP.<sup>3</sup>

Australia's lack of an investment grade energy policy has become a matter of serious political, economic and social concern.

How could this have happened? In the view of the Institute, the politicisation of climate change and environmental issues spilled over to the energy industry, causing an excessive and unnecessary politicisation of energy issues.

This excessive politicisation has created uncertainty for investors; it has resulted in discriminatory policy treatment towards competing energy technologies, with governments picking winners and losers; it has created an uneven playing field with unpredictable rules; it has induced the energy industry to fracture into rival interests, forcing them to compete for subsidies or for favourable policy treatment; and it has provoked disquiet and mistrust in the community. There is also a lack of appreciation in the community about the central role of fossil fuels in energy supply and their continuing long-term importance to global economies.

This has led to high electricity and gas prices for consumers and a high level of political risk for investors. Providers of finance for investors find it hard to assess and price political risk. Some will not accept it at all and, when they do, they tend to write it into their financing arrangements as a 'material adverse risk' for which borrowers are responsible, with the possible consequence of triggering early repayment.

#### ***Recommendation 2:***

***Excessive politicisation of energy issues must be effectively addressed, otherwise energy policy will remain irrelevant. A process of depoliticisation and stakeholder participation is the key to achieve policy reliability and predictability.***

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<sup>3</sup> Robert Pritchard, "Searching for Realistic Pathways in a New Energy World: An Initial Commentary on the Australian Energy White Paper", Energy Policy Institute of Australia, 16 December 2012 – [click here](http://www.energypolicyinstitute.com.au) or go to [www.energypolicyinstitute.com.au](http://www.energypolicyinstitute.com.au).

The problem of excessive energy politicisation is not confined to Australia. However, as a country with very heavy dependence on energy for its wealth creation, its economic development and its export revenues, and with a challenging federal system of government, it is essential for Australia to treat the problem with the utmost seriousness.

The Institute's approach to the process of depoliticisation is outlined in Part 2 of this submission.

### ***Energy innovation***

In energy policy formulation, it is all too easy to be side-tracked by short-term tactical issues and to overlook, or not even recognize, the underlying policy shortcomings. For the EWP Issues Paper not to seek specific submissions on energy innovation policy may be a sign of this.

In policy terms, energy innovation is essential for the achievement of an integrated, coherent energy policy.<sup>4</sup>

#### ***Recommendation 3:***

***Energy innovation policy must be an essential component of energy policy.***

### ***Technology neutrality***

Technology neutrality is an article of faith for the Institute. It is imperative that all energy technologies be able to compete for investment funds on a level playing field.

#### ***Recommendation 4:***

***Technology-neutrality is a fundamental principle of energy policy; all energy technology options should be able to compete on their economic and environmental merits in an efficient market with predictable rules.***

### ***Excessive detail***

An energy policy that degenerates into excessive detail will not be sufficiently robust to survive the changing dynamics of global and domestic energy markets, nor electoral cycles, and will quickly be weakened. The Institute emphasises the need for straightforward policy principles that will stand the test of time.

#### ***Recommendation 5:***

***Energy policy should be in the form of objectives and principles that enjoy bipartisan support and hence are observed. Detailed policy responses by successive governments should conform to these principles.***

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<sup>4</sup> Energy innovation policy is addressed in further detail in Part 7 of this submission.

### ***High energy prices, and the impact on the broad economy***

The Energy Policy Institute is concerned at the affordability of energy and the impact of high energy prices on all consumer classes and the broad economy. High energy prices are forcing industry to migrate to a high energy cost base and triggering a major reassessment of all energy-intensive and energy cost-exposed businesses. To control energy price rises, it is essential that competitive markets are open to all would-be competitors and are allowed to operate efficiently.

#### **Recommendation 6:**

**Affordable energy prices are best achieved by the efficient operation of competitive markets. In the case of monopoly network services, economic regulation should as far as possible seek to mimic the effects of competitive markets and result in efficient price outcomes.**

This introduction has spelt out the Institute's first 6 policy recommendations.

The following Parts 1 to 7 of this submission track the seven chapter headings foreshadowed by the EWP Issues Paper and contain a further 20 recommendations.

## **PART 1: THE SECURITY OF ENERGY SUPPLIES**

As elaborated in Part 7 of this submission; all power generation options, including nuclear power, have a part to play in providing security of energy supply. The Institute's comments on all of the issues raised in Parts 1 to 7 of the Government's issue's paper follow.

### **1.1 *Ways community expectations can be better understood and reflected in network reliability standards***

The level of network reliability and the methodology for determining reliability currently varies from state to state. For example, across jurisdictions, differing levels of contingency events are planned for and deterministic and probabilistic approaches to planning are used. Methodologies for setting reliability standards, planning for reliability and measuring and reporting should be transparent and consistent across jurisdictions.

The AEMC has recently completed reviews under the direction of the Standing Committee on Energy direction on National Frameworks for Transmission Reliability and Distribution Reliability. For each review the AEMC recommended a framework to promote greater efficiency, transparency and community consultation on how reliability levels are set. The AEMC recommendations should be implemented expeditiously and responsibilities should be centralised as much as possible. These reliability reforms, along with other rule changes currently being implemented on network regulation, including the economic returns that networks earn, and increased scrutiny on expenditure proposals will help manage future price increases and give customers greater confidence in energy market institutions.

#### **Recommendation 7:**

**Nationally consistent network reliability levels and increased regulatory scrutiny of expenditure proposals are necessary to satisfy community expectations about the reliability and affordability of electricity supply.**

### **1.2 *The value of developing fuel reserves to meet Australia's international oil security obligations, and augment domestic security***

Reserve stocks are an essential short-term buffer against interruptions to supply but are best left to market participants to make their own arrangements. The Institute believes that the efficient operation of competitive energy markets will provide security of supply at affordable prices.

#### **Recommendation 8:**

**Australia's oil security requires both supply-side and demand-side policies; on the supply-side, an all-out effort is required to encourage domestic oil exploration and reduce reliance on imports; on the demand-side, all transport fuels should be able to compete on their economic and environmental merits.**

The work of Geoscience Australia is of critical importance to this effort and should be bolstered.

Increasing supply is fundamental for Australian security, will improve the efficiency of petroleum markets, and should be further encouraged by government.

### **1.3 Ways to increase new gas sources to meet demand and measures to enhance transparency in gas markets**

The main policy issue here is that insufficient gas resources are being brought to market quickly enough to avoid price hikes and shortages.

As outlined in an Institute Public Policy Paper in June 2013,<sup>5</sup> Eastern Australia, mainly New South Wales, faces a potential gas supply crisis. There is plenty of gas in the ground but it is too often blocked from getting into any market by a combination of regulatory, environmental and social constraints that have created an investment imbroglio. Some elements of the gas industry contributed to the problem in the early days by not appreciating and not adequately responding to community concerns. As the policy paper explained:

*“Australia is an energy-rich country. This may in part explain why, for many years, eastern Australian consumers have been complacent about their security of supply of gas and its relatively low cost. Their complacency is, however, now being replaced by disquiet, even fear.*

*Central to these concerns is the apparent inability or unwillingness of governments, on whom consumers have depended to look after their energy interests, to develop a forward perspective of unfolding problems and to take effective, timely action to address them. It is related to the broader criticism leveled at governments by the Energy Policy Institute last year that Australia lacks an ‘investment-grade’ energy policy, i.e. a well- balanced, robust and stable policy to attract investment and manage regulatory risk in the energy industry.*

*Gas consumers in eastern Australia, principally in New South Wales, are now faced with potential shortfalls in supply and very large increases in prices as a result of, first, the pressure from the export of coal seam gas (CSG) as LNG and, secondly, the inability of successive New South Wales governments to come to terms with the implications of existing contracts from interstate suppliers ‘rolling off’ from the middle of this decade.*

...

*It seems to be ‘the Australian way’, when faced with a substantial problem, to reach for a committee, and often further complicate the situation by running federal and state inquiries separately. This is exactly what is happening in the current situation.*

Action is required to remove blockages – not further inquiries.

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<sup>5</sup> Robert Pritchard and Keith Orchison, “*Getting Gas to Market – Any Market*”, Energy Policy Institute of Australia, Public Policy Paper No 3/2013, June 2013 (underlining provided).

**Recommendation 9:**

***Additional gas resources must be quickly developed and brought to market. The current gas policy failure in New South Wales should be addressed by a well-resourced, action-oriented task force involving all affected stakeholders to proactively eliminate the blockages, much as has been done in South Australia. There is no need for further inquiries or reports.***

**1.4 Issues relating to the regulation of energy infrastructure.**

The AER State of the Energy Market 2013 report published in December 2013 noted that electricity prices rose nationally over the five years to 2012-13 by 87 per cent in nominal terms. Network costs have been the main contributor to these very large price increases. Network price determinations are set in advance generally for five year periods. Although much of the investment is important in order to meet growth and reliability standards and replace ageing infrastructure, it appears that in recent years there has been over-investment in electricity networks and household and business customers are suffering as a result.

In hindsight, setting capital programs in the pre-Global Financial Crisis world of 2008 that still apply in the current 2013/14 year, as is the case in NSW, would inevitably result in large forecasting errors. The financial impact of over-forecasting has been compounded by economic regulation that has allowed network businesses to earn well above what most analysts would consider a normal economic return. Governments and regulators are seeking to address the issues that have resulted in high levels of network investment and concomitant electricity price increases. Rule changes to rein in returns and give the regulator increased powers to scrutinise and amend capital projects are welcomed but it may take years of more prudent price increases to restore the public's confidence in regulation of the electricity industry.

**Recommendation 10:**

***To ensure reliability of supply, the economic regulation of monopoly network assets should allow for an adequate return on investment but this should not exceed the prevailing risk – adjusted return justified in the market. Regulators should also have some way of influencing what investments should be made.***

## **PART 2: REGULATORY REFORM AND ROLE OF GOVERNMENT**

### **2.1 *Priority issues, barriers or gaps both within and outside the energy market reform agenda of the Council of Australian Governments (COAG) – where policymakers have failed to enunciate clear vision for energy policy and to win community trust.***

In the view of the Institute, Australia's energy policy has been rendered irrelevant. It is a type of democratic malfunction with regard to energy policy formulation.

There are three main explanations for this. The first is that, by and large, Australian policymakers have failed to enunciate a clear vision for energy policy, provide confidence in the efficiency and robustness of the energy system, and win community trust .

The second explanation relates to the limitations of 'cooperative federalism' as it has evolved under COAG. It is a problem unique to Australia.

The third explanation relates to the universal shortcomings of representative systems of government as efficient regulators of the modern energy industry.

We address each of these in turn.

#### **(i) *The failure of Australian policymakers to enunciate a clear vision for energy policy, provide confidence in the efficiency and robustness of the energy system, and win community trust***

The Institute cannot emphasise more strongly the view, expressed in its first submission to the EWP process, that a nationally agreed energy vision is the central requirement of any energy policy. Further, energy policy must be integrated horizontally across other policies and vertically amongst all levels of government, if it is to be coherent and intelligible to industry and the public. A bipartisan approach will work best.

The excessive level of politicisation of energy issues must be effectively addressed by broad agreement on the key principles of energy policy. Energy policy formulation not only needs to be undertaken in a more timely fashion but also needs to be pursued over the long term in an apolitical, transparent and participative manner, involving industry, the broad community and all key stakeholders, especially if it is to hold their trust.<sup>6</sup>

#### **Recommendation 11:**

***A nationally agreed energy vision is the central, indispensable requirement for an integrated, coherent energy policy, in order to secure acceptance of the key principles of energy policy, reduce the excessive level of politicisation of energy issues, and build community trust. Its starting point should be the commencement of a genuine process of stakeholder participation. It cannot be completed simply by calling for submissions and publishing an EWP and it will need to be methodically pursued over the long term.***

<sup>6</sup> Robert Pritchard, "Trust and Energy Governance in Australia," Energy Policy Institute of Australia, Public Policy Paper No 1/2013, June 2013.

(ii) ***'Cooperative federalism' as it applies to the energy industry is not always cooperative***

The obvious explanation for the limits of 'cooperative federalism' is that too many Parliaments are involved and none of them has undivided accountability to a single electorate for what they collectively decide. It lacks any constitutional foundation. This constitutes a significant democratic malfunction, the cause of which requires to be acknowledged and the consequences of which require to be addressed.

The Institute reiterates that energy policy formulation cannot succeed behind closed doors. The so-called comprehensive reform agenda of the COAG process of consultation amongst governments, each with their own agendas, can never be a substitute for a wholly-inclusive, intelligible and well-rounded approach towards the formulation of energy policy. Without such an approach, in the view of the Institute, there can never be an integrated, coherent energy policy in Australia and we will all continue to fool ourselves that we have one.

'Cooperative federalism' was justifiably praised for the national energy market reforms, when the participating governments bound themselves together by the Australian Energy Market Agreement (AEMA) in 2004. However, any of them can withdraw on 12 month's notice.

The COAG energy reform process has been slow from the beginning; it has been a process of fits and starts; it has noticeably lagged in recent years, most manifestly in electricity network regulation and in gas supply; and its processes are excessively political.

One of the less satisfactory outcomes of the COAG reform process has been that the NEM is regulated at national level by three regulatory agencies: the ACCC, the AER and the AEMC, with inevitable regulatory overlap. The three agencies negotiated an inter-agency agreement on how they would cooperate with each other but areas of overlap and ambiguity remained. Recently, COAG's Standing Council on Energy (SCE) decided that the AER should become independent of the ACCC.

In summary, it can be said of COAG that:

- it has no institutional identity
- it does not have a high level of transparency
- it has no accountability to anyone except itself
- its decision-making is excessively political (impossible to eliminate when COAG is a Commonwealth-State political body whose representatives change as governments change)
- its decision-making process is protracted and slow to respond
- its agendas tend to be concerned only with the most pressing issues of the time and
- it has no permanent secretariat or dedicated resources of its own.

At the last meeting of COAG on 13 December 2013 (its 36<sup>th</sup>), its members issued a communiqué saying amongst other things that *"too much bureaucracy and red tape has grown up around COAG [and that] its Council system should be streamlined and refocused on COAG's priorities over the next 12-18 months."* Now the question after all this time is whether the SCE as presently configured could really be reformed and streamlined. We strongly doubt this. We suggest it may be more appropriate for all stakeholders to have a say rather than turn the problem back again to the officials of the participating governments for them to try to sort it out behind closed doors.

Some policymakers may hold the belief that COAG can again become an efficient and effective instrument of government reform responsive to modern industry and community requirements.

Long-term reliance on the responsiveness of the COAG process for domestic energy market reform would in our view be misplaced - too much has changed in global and domestic energy and financial markets. As well, the public is now very wary of having the wool pulled over its eyes by governments; it is far better educated about politics than it was a decade ago; and it is wishing to avoid second-best political outcomes in which it has played no effective part.

**Recommendation 12:**

***The implementation of Australian energy policy should be improved to achieve greater consistency and effectiveness. This should be addressed by:***

***(i) Elevating the essential objectives to:***

***a) promote a conducive investment climate in Australia, in which capital can be safely invested and in which the interests of all stakeholders, including energy consumers, are taken into account, and***

***b) arrest the slide of Australian industry towards international uncompetitiveness;***

***(ii) Creating a permanent, fit-for-purpose, independent national institution, with appropriate resources and predictable and transparent processes, accountable not only to jurisdictions but also to stakeholders, to formulate, implement and review Australian energy policy and energy market reforms over the long term;***

***(iii) Undertaking regular reviews of progress in implementation; and***

***(iv) Providing for genuine stakeholder participation and an appropriate degree of accountability at all stages of the policy formulation, implementation and review.***

The likelihood that the development of an independent institution will involve trade-offs and costs for governments and other stakeholders is no reason to cling to what we consider to be a sub-optimal *status quo*.

The advantages to all jurisdictions and stakeholders, including the community, would be to provide:

- greater efficiency
- a greater unity of national purpose
- a greater degree of policy predictability
- a greater degree of transparency
- a reduced risk of market intervention
- reduced regulatory risk and
- a greater level of accountability.

As to the legal implications of this recommendation, it is apparent that the Commonwealth has unilateral power to legislate to govern national energy markets both under the 'trade and commerce power' and the 'corporations power' in s 51 of the Australian Constitution.

The corporations power gives authority to the Commonwealth to make laws with respect to 'foreign corporations, and trading or financial corporations formed within the limits of the Commonwealth' (known collectively as 'constitutional corporations'). This enables the Commonwealth to regulate energy trade in so far as it interacts with all such corporations.

The scope of the corporations power was tested In the 2006 *Work Choices* case when the High Court endorsed the view that the corporations power extends to:

*“... the regulation of the activities, functions, relationships and the business of a corporation described in that sub-section, the creation of rights, and privileges belonging to such a corporation, the imposition of obligations on it and, in respect of those matters, to the regulation of the conduct of those through whom it acts, its employees and shareholders and, also, the regulation of those whose conduct is or is capable of affecting its activities, functions, relationships or business.”*  
(underlining provided)

Most State-owned utilities have been corporatised and operate at arm’s length from the States, falling within the definition of constitutional corporations and subject to the reach of Commonwealth legislation. Many of the former utilities have also been privatised, mainly in Victoria and South Australia.

Although certain constraints operate on the exercise of Commonwealth power, legislation can be framed so as to protect the legitimate interests of the States. For example, no Commonwealth law - of trade or commerce or otherwise - may interfere with the directive in s 92 of the Constitution that *‘trade, commerce, and intercourse among the States ... shall be absolutely free’*. This has been interpreted so as to strike down laws that are discriminatory in a protectionist sense, such as by imposing levies on the States. In addition, the Commonwealth may not under s 99 pass a law relating to trade or commerce that gives preference to one State over another and the Commonwealth may not under s 114 pass a law that has the effect of utilising or attacking State property.

We believe that the lack of accountability for the efficient regulation of the national energy industry that is inherent in the current COAG arrangements could be addressed by Commonwealth legislation without diminishing the legitimate interests of the States.

**(iii) *The universal shortcomings of governments as efficient regulators of the modern energy industry***

The modern energy industry is almost entirely driven by market forces but energy markets remain very vulnerable to arbitrary intervention by governments. In this regard, stakeholder engagement is required of policymakers to foster efficient markets, to address the national and global energy challenges and to provide the necessary ingredient of political bipartisanship. Stakeholder engagement is not something that happens automatically – it requires an institutional process.

**Recommendation 13:**

***Governments should determine the energy policy vision, and rely on markets to allocate resources to deliver efficient outcomes. Intervention in any market should be confined to instances of clear market failure and should be limited to what is necessary to remedy the failure.***

As the Institute outlined in a Public Policy Paper in 2013:

*“Genuine public participation requires a mechanism for responding to concerns; not just perfunctory consultation. In recent years, Australia has been swamped by so many public consultations and inquiries that neither industry nor the public has been able to accept them as entirely genuine. There is considerable public cynicism whether the views of those consulted were given serious consideration. In addition, inquiries at parliamentary level have often failed to achieve consensus, tending to reinforce public doubt and mistrust.*

*The contemporary economic and public interest demands that greater emphasis be paid to genuine public participation. This could be accommodated in the case of the Australian energy industry by a well-resourced, independent institution with a governing board on which industry and the public are represented. Its charter would be to make recommendations to governments on policies for the efficient, safe, secure, environmentally sound and competitive energy supply to the Australian economy and to the public. It would conduct independent reviews and make recommendations on appropriate policy responses to issues as they arise.*

*Representatives could serve for limited periods and be replaced at regular intervals. An independent institution would have long-run objectives for which its governing board would be accountable; it would be required to report annually to the Commonwealth and State governments, to industry and to the public on its deliberations and recommendations; it would need to be open and transparent in all of its deliberations; and it could conduct 'listening sessions' on issues of particular importance.*

*Participative processes can and must be undertaken in a trustworthy, fair, non-discriminatory and technology-neutral manner. A fit-for-purpose model could be designed for Australia's particular needs, taking a pragmatic approach and focusing on forging unity of national purpose. Other federal countries provide precedents for strong, independent energy bodies, such as the National Energy Board and Nuclear Safety Commission in Canada and the Federal Energy Regulatory Commission and the Nuclear Regulatory Commission in the United States."<sup>7</sup>*

We query whether the SCE would ever be willing to undertake or be capable of undertaking an institutional monitoring and review process to accommodate the legitimate concerns of industry, the community and key stakeholders. The establishment of an independent National Energy Commission may be the only effective solution.

## **2.2 Possible approaches and impacts of review of tariff structures including fixed network costs, further time-of-use based electricity tariffs and the use of smart meters**

It is an important principle that electricity tariffs should reflect economic costs to enable customers to make informed choices with respect to electricity consumption and substitution decisions. Smart meters will greatly increase the potential to provide time-of-use pricing to customers that reflects the changing economic cost of producing and delivering electricity over hourly, daily and seasonal timeframes. Smart meters also open up the possibility of more innovative products such as critical peak pricing, real time pricing and load control as a response to price signals.

The deployment of smart meters has been slow in part due to a lack of standards, regulatory uncertainty and a negative reaction to the mandated roll-out of smart meters in Victoria. Governments should facilitate a customer and market driven roll-out of smart meters in order to provide behavioural signals to customers that minimise investment costs and overall price increases.

It is likely that it will take many years for smart meters to be fully deployed. In the meantime tariff structures must be responsive to market developments. Driven by overly generous subsidies, growth in solar PV systems has been extraordinary with installed capacity increasing 100 fold over the past five years from 30 MW in 2008 to 3000 MW at the end of 2013, according to the Clean Energy Regulator. Rooftop solar PV now competes well with retail electricity prices even with no subsidies. However, the existing network tariffs effectively provide an additional unnecessary subsidy from those who don't have solar to

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<sup>7</sup> Robert Pritchard, footnote 2 above.

those that do. Network tariff reform by increasing fixed costs to reduce the subsidy flowing to solar PV owners is important on an equity basis and to enable decisions to install solar to be fully informed and rational.

### **2.3 Possible measures to promote greater price transparency in gas markets**

Policy reforms in recent years that have increased price transparency in gas markets. These reforms include the implementation of Short Term Trading Markets in Sydney, Adelaide and Brisbane and the gas supply hub under development for Wallumbilla in Queensland, due to be commissioned in 2014. The SCE is also considering policy options to increase trade in gas transmission pipeline capacity. These market reforms should be built on incrementally where there are clear benefits but they should not be a substitute for the removal of regulatory barriers that discourage the early development of gas reserves for domestic consumption and potential export as LNG.

### **2.4 Areas where further privatisation of government-owned assets would contribute to more effective regulatory frameworks and better outcomes for consumers**

With appropriate economic and technical regulation of network assets to prevent monopoly rent-seeking behavior by asset owners that provides for consumer and other stakeholder participation, and where private capital is available, we do not consider that there is any purpose in governments retaining ownership of any energy assets. Further, there are irreconcilable conflicts of interest between the desire to generate revenue and the objective of providing electricity to consumers at the lowest cost.

The efficient exploitation of Australia's fossil energy resources, particularly coal, for the benefit of the nation requires access to infrastructure to transport the primary energy source to markets. Australia's energy policy should articulate policy objectives and strategies to ensure the availability and operation of required infrastructure in a manner that supports energy product exports.

## PART 3: GROWTH AND INVESTMENT

The Institute reminds government of the comprehensive suite of recommendations on energy financing advanced by KPMG and the Energy Policy Institute in a joint paper in March 2013.<sup>8</sup> A total of 28 recommendations reflecting four themes were identified in chapter 5 of the KPMG / Institute paper:

- removing market impediments to financing innovation;
- developing a better energy market framework to improve the energy investment environment and attract finance;
- creating an 'investment grade' energy policy; and
- the corporate sector moving to a more integrated reporting model to support investment decisions.

Four recommendations from that paper are addressed elsewhere in this submission.<sup>9</sup> Five other recommendations are contained in Parts 3 and 4 of this submission and correlate to Australia's ambitions in leading the G20 and B20 in 2014.

The Prime Minister has emphasised attracting private infrastructure investment as a key strategy to stimulate growth in launching Australia's G20 year. He specifically identified the essential importance of well-functioning energy markets and reliability of supply.<sup>10</sup>

The table below summarises the KPMG / Energy Policy Institute growth and investment-specific recommendations, cross-references them to Parts 3 and 4 of this submission, and links them to the 2014 G20 and B20 priorities:

KPMG / Energy Policy Institute Recommendation	EPI EWP Submission (Part / Recomm'n)	G20 / B20 2014 Priority
1 Address the reasons for superannuation fund trustees' reluctance to invest in long term energy projects	3.1 / 12.1	<ul style="list-style-type: none"> <li>• Attract private infrastructure investment (G20)</li> <li>• Promote a broad range of financing instruments and sources (B20)</li> <li>• Review and suggest improvements to make reporting model more conducive to investment (B20)</li> </ul>
2 Develop Australian debt markets, including the bond market	3.1 / 12.2	<ul style="list-style-type: none"> <li>• Attracting private infrastructure investment (G20)</li> <li>• Promote a broad range of financing instruments and sources [including taking the necessary steps] to develop corporate bond markets as an alternative to bank financing (B20)</li> <li>• Review and suggest improvements to make</li> </ul>

<sup>8</sup> KPMG and The Energy Policy Institute of Australia, "Australia's Energy Financing Challenge", March 2013 - [click here](#) for a copy or go to [www.energypolicyinstitute.com.au](http://www.energypolicyinstitute.com.au). The recommendations were derived from an extensive process of consultation with energy and finance sector stakeholders and remain well-founded.

<sup>9</sup> Two recommendations about creating an investment grade energy policy (Reform current regulation at federal and state levels including the COAG and SCER processes; Regularly assess and provide a consolidated view of the energy investment pipeline) are addressed in Part 2.1 (Recommendations 11 and 12) of this submission. Recommendations about developing a better energy market framework (Privatise all generation energy assets; facilitate demand side participation) are addressed in Parts 2.2 to 2.4 of this submission.

<sup>10</sup> The Hon Tony Abbott MP, Prime Minister of Australia, 'G20 2014: Overview of Australia's Presidency', December 2013

KPMG / Energy Policy Institute Recommendation	EPI EWP Submission (Part / Recomm'n)	G20 / B20 2014 Priority
		reporting model more conducive to investment (B20)
3 Move to a more integrated reporting model to support investment decisions	3.1 / 12.3	<ul style="list-style-type: none"> <li>Review and suggest improvements to make reporting model more conducive to investment (B20)</li> </ul>
4 Develop an integrated report across the Australian energy sector	3.1 / 12.4	<ul style="list-style-type: none"> <li>Create freer energy markets through stable, rational policies (B20)</li> <li>Review and suggest improvements to make the reporting model more conducive to investment (B20)</li> </ul>
5 Consider various tax changes to level the global playing field	4.2 / 15.2	<ul style="list-style-type: none"> <li>Remove obstacles to trade (G20)</li> </ul>

**Recommendation 14:**

***The 28 recommendations identified by the KPMG/Energy Policy Institute energy financing paper in March 2013 should be implemented. The Department of Industry should involve Treasury in the Energy White Paper process and in its policy deliberations with a view to making this happen as soon as possible.***

**3.1 Commercial or market initiatives that could enhance growth and investment in the energy and resources sectors**

The International Integrated Reporting Council (IIRC) released its Integrated Reporting Framework in December 2013,<sup>11</sup> The Framework could play a role in monitoring and reporting on the implementation of policy by governments across electoral cycles

**Recommendation 15:**

***An 'investment grade' energy policy and a level playing field for all technologies should automatically lead to certain innovation and commercial initiatives. As an aid in pursuing an investment grade energy policy, consideration should be given to:***

- the reasons for superannuation fund trustees' reluctance to invest in long term energy projects;***
- the further development Australian debt markets, including the \$A bond market to increase liquidity and depth;***
- an integrated reporting model to support investment decisions; and***
- an integrated report across the Australian energy sector as a sustainable, cross-electoral cycle tool to monitor progress towards the nationally agreed energy vision.***

**3.2 Areas where approvals processes could be further streamlined while maintaining proper environmental and social safeguards**

<sup>11</sup> International Integrated Reporting Council, "The International Integrated Reporting Framework," December 2013, <http://www.theiirc.org/international-ir-framework/>

Energy resource developments are complex, require multi-billion dollar investments, and have long lives (decades) over which the return on the original investment is delivered.

The complexity, duration, and cost of project approval processes and the number, complexity and cost of conditions attached to project approvals have increased alarmingly in Australia to the point where they now pose a level of sovereign risk that is a significant disincentive to develop Australian energy resources.

Approval processes lack the flexibility required to efficiently regulate dynamic developments such as coal mines (as opposed to static developments such as housing developments). These approvals often prevent mines from responding to market movements in a timely manner (eg, mining the resource in a different order to take advantage of a spike in the price of a particular product). Even though the response would not lead to any increase in project footprint or offsite impact, the miner is required to develop and submit a modification of the existing approval.

**Recommendation 16:**

***There should be a new process to work with State Governments to deliver efficient, effective and flexible approvals processes for the 21<sup>st</sup> century which deliver certainty to the project developer and all other stakeholders. No more than one development approval process and no more than one level of government should be responsible for development approvals. Appeals on points of law, but not on the merits of original decisions, should be allowed.***

**3.3 Further ways that regulatory burdens could be reduced while maintaining appropriate levels of disclosure and transparency in energy markets**

Detailed measures for reduction of other regulatory burdens should flow naturally from 'investment grade' energy policy.

**3.4 The impacts of variable land access policy and ways the community could be better informed and engaged on development in the energy sector.**

The essential requirement in energy development is certainty of process, both for investors and stakeholders.

Genuine public participation is a prerequisite. An institutional process is required, along the lines suggested in Recommendation 11 above.

## **PART 4: TRADE AND INTERNATIONAL RELATIONS**

### **4.1 How to grow the export of value-added energy products and services**

The key concern of Australia's customers is their own energy security and reliability of supply. This is what attracts them to Australia as customers and as upstream investors.

#### **Recommendation 17:**

***Australia must be a reliable supplier to its overseas customers. Energy costs and other input costs to production should be determined by efficient markets.***

### **4.2 Ways to remove unnecessary barriers to continued foreign investment in Australia's energy sector**

Key factors in discouraging foreign investment is Australia's comparatively high level of tax, and the complexity of our regulatory and approval processes.

#### **Recommendation 18:**

***Australian tax rates should encourage not discourage investment. Various tax changes should be considered, including removal of the early 2013 withholding tax increase on managed investment trusts and remedying the inequality of tax treatment for global debt investors receiving interest from bonds.***

Policy overall needs to encourage investment and, in particular, Australia's foreign investment approval procedures should be streamlined and made transparent.

#### **Recommendation 19:**

***Australia's foreign investment legislation is very difficult to interpret and should be clarified. It should clearly encourage foreign investment rather than restrict it.***

### **4.3 Ways to strengthen support for access to export markets**

The Institute offers no specific view.

### **4.4 Ways to support business to maximise export opportunities for Australia's energy commodities, products, technologies and services, including the value of Australia's participation in the variety of international forums**

The Institute considers that:

- Government policy should be focused on removing barriers and impacts on the competitiveness of Australia's energy export industries rather than attempting to prop up uncompetitive industries. However, facilitating excellent relations with trading partners and removing barriers to international trade is certainly an area where government should have a very prominent role.
- Bilateral consultations with key trading partners should be maintained but could be switched to a biennial basis. There should be a mechanism for consultation

with business and greater advance notice should be given.

- Australia's participation in the APEC Energy Working Group should be reinvigorated but meetings should be held annually instead of each six months.
- Australia should maintain active membership and participation in the activities of the G20, OECD, IEA and the IAEA with business involvement.

**Recommendation 20:**

***Australia should renew and intensify its efforts at multilateral, regional and bilateral levels to remove all barriers to international energy trade.***

***There should be an agreed mechanism for business to be regularly consulted in timely fashion about all political and other government initiatives that impact on energy export trade. Business should be afforded greater opportunity to be involved.***

## **PART 5: WORKFORCE PRODUCTIVITY**

### **5.1 *The nature of any current skills shortages being experienced and how these could be addressed by and with industry***

The Institute does not believe this involves an issue of policy that is specific to the energy industry.

### **5.2 *The capacity of industry and education sector-led programs to meet long-term training and skills development needs of the energy and resources sectors***

Again the Institute does not believe this involves an issue of policy that is specific to the energy industry.

### **5.3 *Specific long-term training and skills development needs for alternative transport fuel, renewable energy, energy management and other clean energy industries***

Australia should be an innovative country in the development and utilisation of all energy technologies, maximising research and development within Australia and its ability to quickly adopt and implement the latest technologies from abroad.

The Institute considers that all energy options should be open and be able to compete on a level playing field. Technology neutrality should be an article of faith in training and skills development programmes.

#### **Recommendation 21:**

***Increasing Australian workforce productivity in the energy industry should be strongly supported by government training and skills development support programmes. These should be provided on a technology-neutral basis, utilising domestic research and development and adopting technologies developed abroad.***

## **PART 6: DRIVING ENERGY PRODUCTIVITY**

### **6.1 *The current suite of energy efficiency measures, ways these could be enhanced to provide greater energy efficiency or possible new measures that would enhance energy productivity***

The Institute strongly supports energy efficiency measures where there is a demonstrated market failure but refrains from recommending any detailed additional policy measures.

#### **Recommendation 22:**

***All measures to promote energy efficiency should be made available or applied to all technologies on a technology-neutral basis. Regulation intended to drive energy efficiency should only be promulgated where there is a demonstrated market failure.***

### **6.2 *The use of demand-side participation measures to encourage energy productivity and reduce peak energy use***

The Institute supports these measures as a policy principle but refrains from recommending any detailed policy measure.

### **6.3 *Measures to increase energy use efficiency in the transport sector***

The Institute supports these measures as a policy principle but refrains from recommending any detailed policy measure.

## PART 7: ALTERNATIVE AND EMERGING ENERGY SOURCES AND TECHNOLOGY

### 7.1 *Ways to encourage a lower emissions energy supply that avoids market distortion or causes increased energy prices*

It needs to be understood that emission reduction options, other than some energy efficiency measures that have a net economic benefit, will unavoidably involve increased prices. The lowest-cost measures should therefore be pursued and these should be derived from market based activities.

Technology-neutrality is a fundamental principle of energy policy; all energy production options should be able to compete on a level playing field with predictable rules.

All discriminatory and market-distorting measures should be eliminated. Such measures include, on the one hand, arbitrary renewable targets and, on the other, the banning of fracking processes in oil and gas production and the prohibition of uranium mining and nuclear power production.

As Malcolm Keay of the Oxford Institute of Energy Studies has emphasised in a recent Institute Public Policy Paper, the non-dispatchability of renewables leads to higher system costs:<sup>12</sup>

*“There is really no such thing as “the cost of renewables”. Particular renewable sources, in particular locations, at particular times, within particular electricity systems, all have different costs. Renewable energy depends on natural forces. These forces are stronger at some locations than others and at some times than others so that the cost of, say, wind or solar power will depend on where the plant concerned is built and what time of the day or year it is generating. The costs of electricity generation from different sources are often compared on the basis of what are known as “levelised costs”. These represent the average costs per unit generated during the lifetime of the plant concerned after factoring in (and discounting) all capital, fuel, operating and other costs; they encapsulate all these costs in a single number – eg 5c/kWh. This approach has the advantage of simplicity but can be misleading, particularly when it comes to non-dispatchable plants – ie plants which cannot be called on to produce electricity when the system needs that power.*

*Because electricity is difficult to store, supply and demand have to be kept in balance at all times, so it is vital to have generation capable of adjusting to changes in demand. Most “new” renewable sources are non-dispatchable, because of their reliance on natural forces; they generate when those forces are active and not at other times. As a consequence most “new” renewables lead to an increase in system costs (ie the costs incurred elsewhere in the electricity system to ensure continuing security of supply); the higher the penetration of these renewable sources, the higher the costs imposed on the rest of the power system so, the higher the renewable target a government sets, the more important it is to take full account of these costs. Furthermore, renewable generation has to be sited where the resource is available, rather than where the power is needed, often increasing transmission costs.”*

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<sup>12</sup> Malcolm Keay, “No Such Thing as the Price of Renewables? The Significance of System and Resource Costs”, Energy Policy Institute of Australia, Public Policy Paper No 2/2013, June, 2013. (Underlining provided.)

**Recommendation 23:**

***The lowest-cost emission reductions should be delivered by an efficient market mechanism on a technology-neutral basis. This will minimise the overall burden on the economy; equally importantly, it will enable reductions to be pursued in a competitive and effective non-discriminatory fashion across an open and unobstructed portfolio of energy technologies.***

The functions of the Australian Renewable Energy Agency could valuably be widened to include all low-emissions energy measures, not just renewables.

Energy innovation policy is an essential component of energy policy that was not specifically canvassed in the EWP Issues Paper. We address it here by commencing with a specific recommendation.

**Recommendation 24:**

***A greater value should be placed on energy innovation and greater efforts should be made to support it. The key elements of energy innovation policy should be a portfolio approach to investment in a range of technology options and facilitation of domestic and international collaboration.***

As Professor Chris Greig of the University of Queensland explain it in a recent Institute Public Policy Paper:

*“Policies to force the transition to a low carbon energy sector cannot be sustained without affordable, technologically reliable solutions. Technological innovation is necessary but is universally characterised by patient, high-risk, high-reward investment. This is particularly the case in the clean energy sector where good ideas abound but true innovation through to widespread commercial deployment is rare (e.g. renewable energy with storage and carbon capture and storage). As a result, global achievements in decarbonising the energy sector continue to lag global ambitions.*

*... Australia does not value innovation highly enough.*

*...The relative merits of alternative low-emissions energy technologies cannot be reliably predicted without a significant number of demonstration projects for each technology. Successful innovative organisations deal with this problem by preserving optionality and supporting a portfolio of options. Improving the prospects of low carbon energy technologies should therefore involve innovation and technology enhancement that reduce investment risk and project costs across an appropriate suite of potential low-carbon energy technologies.*

*Individual project failures are inevitable and it is therefore imperative that innovation policy results in a portfolio investment approach. Attempting to pick individual technology winners exposes governments to the risk of a specific failure becoming a political issue and being used to reduce or shut down support for a particular technology, or even the broader clean energy programs.”<sup>13</sup>*

The Institute endorses Professor Greig’s views as elaborated above and his articulation of the aspirational objectives of a national energy innovation policy as quoted below:

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<sup>13</sup> Chris Greig, “Energy Innovation Policy and the Need for a Portfolio Approach,” Energy Policy Institute of Australia, Public Policy Paper No 4/2013, November 2013. (Underlining provided)

*“A national energy innovation policy must result in improved education and training to maintain a competitive advantage as well as to pursue internationalisation through mobility. This should focus on attracting R&D talent to Australia and fostering a culture of globally connected researchers to encourage inward streams of investment, information and skills.”<sup>14</sup>*

**7.2 The need to review existing network tariff structures in the face of rapidly growing deployment of grid-backed-up distributed energy systems, to ensure proper distribution of costs**

The Institute’s views on network tariffs are set out in sections 1.1, 1.4, 2.2 and 2.3 of this submission.

**7.3 Additional cost-effective means, beyond current mandatory targets and grants, to encourage further development of renewable and other alternative energy sources and their effective integration within the wider energy market**

***Allowing all energy options to compete***

The overriding policy principle should be to allow all energy options to compete on a level playing field. In choosing between different low-carbon technologies at different locations, the reduction of greenhouse gas emissions at the lowest cost is the criterion that matters the most.

***Recommendation 25:***

***All power generation options need to be considered within an effective market framework based on economic and environmental merit.***

***Public education***

We believe there is insufficient appreciation by policymakers and in the wider community of the current and future role of competing energy sources in the domestic and global energy economies and their emissions reduction potential. We consider that government has an important role to play in increasing the level of public awareness through education programmes.

***The role of renewables***

Investment in solar, wind and other ‘new’ renewables, as well as storage systems, continues to increase. Despite their well-understood intermittent characteristics in power generation, there is a high level of bipartisan and community support in Australia for renewable power technologies, especially solar, and such support should be given its full weight in the development of energy policy. The stability and resilience of the electricity supply system as a whole is nonetheless of overriding importance if energy supply is to remain reliable and affordable. This again underscores the need for a nationally agreed energy vision as central in the development of sound energy policy.

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<sup>14</sup> Chris Greig, supra.

### ***The role of coal***

Coal remains critical to global energy supply and will remain so for many decades. It is also likely to remain critical to energy supply in Australia.

Low emission coal technologies have an important role in reducing greenhouse gas emissions. In a recent public policy paper for the Institute, Ian Cronshaw, a consultant with the International Energy Agency, concluded:

*“Together, the widespread adoption of more efficient coal power plants and of CCS would make an important contribution to tackling climate change. The success of governments globally in encouraging greater energy diversity, improved efficiency, and the development and deployment of clean coal technologies will have a profound bearing on the role of coal in the longer term.*

*In almost any conceivable scenario, coal will remain a critical part of the power sector in both OECD, and increasingly, non-OECD countries, based on massive recent investments in coal fired plant, plus the widespread availability of secure, affordable supplies.”<sup>15</sup>*

### ***The role of nuclear power***

Nuclear power is used in over 30 countries. We believe that the barriers to nuclear power generation in Australia should be removed to enable it to be considered as a future generation option. Nuclear power produces almost zero emissions and is fully dispatchable, in contrast with renewables which rely on natural forces and tend to be intermittent.

Nuclear power should be regulated by the independent and highly competent regulatory agency, the Australian Radiation Protection and Nuclear Safety Agency (ARPANSA) in accordance with best international practice.

There are significant technological advances in safe nuclear power generation. In particular, factory-produced, small modular reactors (SMRs) are faster to install and are less capital-intensive than the larger, traditional nuclear power plants. SMRs are considered suitable for powering mines and towns in remote locations in many parts of Australia. Additional modules may be installed in an incremental fashion if extra capacity is required.

#### **Recommendation 26:**

***The continuation of the prohibition of nuclear power generation in Australia is unnecessary and should be removed; the powers of ARPANSA as independent regulator should be broadened to cover all developments throughout Australia; although ARPANSA is already accountable by law for its performance as a safety regulator, there should be public participation in its activities in the public interest.***

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<sup>15</sup> Ian Cronshaw, “The Current and Future Role of Coal in the World Energy Economy,” Energy Policy Institute of Australia, Public Policy Paper No 1/2014, January 2014.

**7.4 How the uptake of high efficiency low emissions intensity electricity generation can be progressed**

The Institute considers it is important for policymakers and all stakeholders to develop a fully informed understanding of the current and future role of all energy options and their likely cost. In this regard, we endorse the annual process involving relevant expert stakeholders, building upon data from actual energy projects to maintain a current understanding of energy technology costs undertaken by organisations such as the Bureau of Resources and Energy Economics<sup>16</sup>.

Energy innovation should be an element of Australia's energy policy to drive cost reduction and commercialisation of high efficiency, low emissions intensity technologies. It is noted in this regard that the Renewable Energy Target is not an energy innovation policy; rather, it subsidises the deployment of commercially available technologies that may not be otherwise competitive.

**7.5 Any barriers to increased uptake of LPG in private commercial vehicles and CNG and LNG in the heavy vehicle fleet**

The Institute offers no specific comment on this topic.

**7.6 Any barriers to the increased uptake of electric vehicles and advanced biofuels**

The Institute offers no specific comment on this topic.



Robert Pritchard  
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**Energy Policy Institute of Australia**

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<sup>16</sup> BREE, "Australian Energy Technology Assessment," Canberra, 2013