THE GREENHOUSE CHALLENGE FOR ENERGY

Submission to the Victorian Government

By the Victorian Minerals & Energy Council

18 July 2003

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1. THE MINERALS AND ENERGY INDUSTRY IN VICTORIA

The Victorian Minerals & Energy Council Inc is the industry association that represents the corporate minerals industry, including energy minerals, of Victoria. The members of the Council are engaged in mineral processing, mining, exploration, or the provision of services to the industry.

Victoria has a very important minerals and energy industry that is not only significant nationally but also critical to many other industries in Victoria that depend upon low cost, reliable energy. It also provides significant employment in regional Victoria.

The minerals industry of Victoria:

- Produces more than 65 million tonnes of coal per year;
- Produces about 4 tonnes of gold per year;
- Produces 85% of Victoria's electricity (and 19% nationally);
- Produces titanium minerals;
- Has an annual turnover in Victoria of more than $600M; and
- The mining industry alone directly employs more than 5,000 Victorians (and more than 10,000 indirectly), the majority of these being located in regional Victoria.

The minerals industry is a primary producer of energy minerals and a significant user of energy for mining and downstream processing. The future development of our industry is dependent upon the continued production of energy minerals and access to low cost reliable energy sources. It should also be noted that the minerals industry is committed to the principles of sustainable development. Therefore, we are more than interested in the current debate on the options to curtail greenhouse gases and develop Victoria's natural mineral advantages.

2. GREENHOUSE GAS ABATEMENT POLICIES

The Victorian Greenhouse Strategy has been developed in recognition of the environmental threat posed by climate change, and of the need for an effective response. The goals of the strategy are:

- To build awareness and understanding of climate change issues;
- To limit Victoria's greenhouse gas emissions and enhance greenhouse sinks;
- To position Victoria to prosper in a future carbon constrained economy – including the creation of an environment in which Victorian industry can take advantage of the business opportunities in such an economy; and
- To develop a greater understanding of climate change impacts and, where appropriate, initiate adoption actions relevant to Victoria.

The Bracks Government has a stated aim of achieving its commitments to reduced greenhouse gas (GHG) emissions from energy supply and use, while also maintaining a secure, efficient and affordable energy supply.

The Commonwealth Government's approach to the climate change and GHG abatement strategies can be summarised as:

- Ratification of the Kyoto Protocol is currently not in Australia's best interest, determined in socio-economic terms; and
- Australia will meet its international commitments to a net 108 per cent of 1990 emission levels over the 2008-12 first commitment period of the Kyoto Protocol irrespective of whether Australia is a signatory to it.

We believe that it is important that Victoria's response to climate change and GHG abatement continues to be considered as part of a broader Australian and global solution. The minerals industry supports the need for all parts of the Australian economy to make an equitable contribution to the international effort to reduce GHG emissions.

The minerals industry is committed to supporting a global response to managing climate change that will deliver real GHG emissions abatement, that does not undermine Australian industry's international competitiveness and creates real business opportunities.

We believe that Australia's greenhouse response should be coordinated at the national level, take a long-term perspective, maintain the competitiveness of Australian industry and share the burden of GHG abatement equitably across the community. A nationally coordinated approach should curtail the practice of project proponents going jurisdiction hopping to obtain the best incentive from State Government's.

3. RECOGNISING VICTORIA'S COMPETITIVE ADVANTAGES

The minerals industry consider that it is of paramount importance that efforts to reduce GHG emissions do not harm Victoria's competitive power supply which underpins the industrial success of the State. This power supply is based on our endowment of a world-class brown coal resource. Brown coal is the fuel for 85 per cent of Victoria's electricity supply (and 19 per cent of Australia's). We are blessed with huge brown coal resources in the Latrobe Valley with enough coal for 500 years at current demand levels. This coal is readily mined at world best practice costs.

It is also important to note that Victoria's existing brown coal generating plant is operating at best practice and has operational lives of 30 to 50 years. Coal is projected to remain an important source of energy for Australia for the foreseeable future. ABARE recently predicted that coal would fuel 67 per cent of Australia's electricity generation by 2020 and that gas would increase its share from 10 percent to 21 per cent in the same period. It has also been projected by CSIRO that Australia will require between 74 and 102 per cent more electricity by 2020.

In addition to ensuring that our brown coal resources are effectively utilised it is also important that Victoria's natural gas endowment be effectively developed. This includes the exciting prospects for the extraction of coal seam methane from coal deposits in the State.

Melbourne remains a key centre for the global minerals industry with Victoria a leader in the development of mining technology. Nationally, the minerals industry is the only industry to which Australia can claim to be a global leader.

Victoria is home to significant manufacturing industries that have developed over the years. These industries rely on the availability of reliable, low cost energy and employ a significant number of Victorians. They are also the driver for the development of new technologies that keep Victoria at the forefront of this industry.

Any policy fundamentals of the Bracks Government should be aimed at attracting new generating capacity to Victoria. We have significant natural resources and these should be applied to the base load increases in generating capacity required for the future. Victoria should see itself proudly as the powerhouse for Australia. If investors see Government policy as unattractive then generating capacity will move to the State with the most positive commercial outcome. Victoria must use its natural advantage and turn it into a competitive advantage.

Any policy should account for both emissions and sinks and be clear, simple, transparent and workable, this is a big challenge for the Victorian Government but one with huge rewards. In addition, the Government should actively consider incentives for investments that meet GHG emission targets. These could, for example, include payroll tax reductions for plants using new technology or efficiency gains from existing plant. In addition, any policy must acknowledge the gains that have already been made in reducing GHG emissions in Victoria.

4. INSTRUMENTS TO ACHIEVE CHANGE

The Victorian Government discussion paper has identified the following six instruments to achieve a reduction in GHG emissions:

4.1 Tradable Emission Rights

Policy measures that have broad and mandatory coverage and provide flexibility through some form of tradable rights.

Tradable emissions intensity rights and/or GHG emissions trading permits are instruments that will distort energy market competitiveness and if not managed effectively could be subject to degrees of manipulation that is counterproductive to ensuring an adequate, low cost and reliable electricity and gas supply to Victoria. These instruments are not supported at this time and certainly not as part of a unilateral State based system of abatement measures.

If emissions trading is considered; the key matter of allocation for existing GHG emissions requires to be clarified. Are permits to be partly or wholly grandfathered or auctioned and if grandfathered what allocation date will be considered?

4.2 Non-tradable Emission Levies/Taxes

Measures that seek to provide broad and mandatory incentives for greenhouse abatement which are non-tradable.

The VMEC does not support non-tradable taxes or levies such as a carbon tax, energy tax or levies that artificially adjust competitive energy markets. Such imposts are blunt policy instruments that do not guarantee an effective greenhouse outcome. Whilst such instruments send a signal to industry to reduce GHG they are a negative incentive and place the financial gain with the Government and the costs ultimately on the consumers.

4.3 Specific Tradable Incentives

Several abatement schemes seek to stimulate investment in a specific class of energy sources employing tradable instruments. These schemes are typically mandatory.

The Commonwealth Government's Mandatory Renewable Energy Target (MRET) scheme comes at a high cost. We consider that whilst there is a role for renewable energy technologies in Australia's energy policy:

- incentives for the development of renewable energy technologies should be based on efficient, market-based mechanisms that address market failures;
- MRET is a high cost greenhouse measure and a costly way to develop an industry;
- MRET should be on a transitional basis only and not serve to perpetuate inefficiencies and distortions in the market; and
- there should be no expansion of the MRET measure or any mandating of the mix of renewable energy technologies under the measure.

4.4 Non-tradable Abatement Obligations

A range of schemes focus on specific classes of energy production or use and provide abatement incentives or obligations that are non-tradable. Some such schemes are mandatory.

The introduction of GHG emission targets to new exploration and mining licences is a legitimate position for Government to take. However, the quantum of the improvements sought must be carefully considered as these directly impact on project costs and can be a significant deterrent to new investments in the State and development of our natural resource endowment.

Nevertheless, we have very grave concerns where mandatory GHG abatement obligations are applied to existing licences or to energy minerals that have been included in existing licences. It is totally unacceptable to apply new commitments to energy minerals or the use of energy minerals that have been factored into existing investments. This is seen as a considerable sovereign risk issue by licence holders and could dramatically impact on future investment decisions if implemented by Government.

4.5 Voluntary Abatement Targets

Voluntary measures can include the negotiation of abatement agreements by governments and individual energy producers or users.

The VMEC supports voluntary initiatives that establish efficiency standards for plant and equipment and targets for GHG abatement. All of the major company members of the Council are committed signatories to the Commonwealth Government's Greenhouse Challenge and all have achieved significant reductions in GHG emissions as a result. In addition, our brown coal members operate their generating plant at best practice as monitored by the Commonwealth, all fully support and participate in the Generation Efficiency Standards, and all are signatories to the Australian Minerals Industry Code for Environmental Management.

4.6 Government Funding Initiatives

Governments may also provide funding to particular firms or bodies to develop or implement abatement technologies.

The VMEC considers that one of the most effective instruments for long-term solutions to GHG abatement is through the introduction of new technologies, funded through bidding systems as appropriate. The technology solution to climate change requires the support of Government and should include R&D into emission reduction and thermal efficiency improvement for thermal power plants as well as R&D for renewables.

Government support for the CRC for Clean Power from Lignite is acknowledged but considered by VMEC to be far too small. In addition, the Coal21 Project being managed by the Australian Coal Association with an aim to identify technologies that will achieve zero emission is supported by Government and we would hope that implementation of the findings receive financial support in the future.

International collaboration in the development of these technologies will be required to lower costs. The new CRC for Greenhouse Gas Technologies and Government support for the carbon sequestration leadership forum are worthy initiatives that should be further supported.

The successful implementation of the new technologies is critical to Victoria continuing to benefit from the wonderful endowment of low sulphur, low ash (but high moisture) brown coal.

5. SUSTAINABLE DEVELOPMENT ISSUES

Energy underpins the economy and living standards of Australia, servicing households as well as commerce and industry at some of the world's lowest prices. It provides significant direct and indirect employment, substantial investment opportunities and, particularly through energy related exports, substantial export earnings. Energy intensive industries make a major contribution to the national GDP.

However, a critical strategic issue facing the minerals industry is the necessity for a highly competitive, nationally integrated electricity and gas market. A consistent whole of government approach, which is integrated within government, will be necessary if a sound outcome is to be achieved. This will require:

- Energy to be considered in its totality;
- A national competitive market governed by nationally consistent regulation of generation, transmission and distribution/retail;
- Full and comprehensive consideration of GHG abatement based on sound principles of sustainable development; and
- Direct efforts to improve the efficiency of energy markets in a manner that is not undermined by ill-considered policies on and/or lack of reforms in some areas.

The VMEC seeks the establishment of a nationally consistent system of energy regulation and governance, open and contestable markets, adequate and integrated infrastructure, and the reform of piecemeal, discriminatory and poorly targeted GHG abatement measures.

Continuing reliable, competitively priced energy supply is critical to the success of the national economic reform agenda and to the maintenance and improvement of the minerals sector's, and other energy intensive sectors, domestic and international competitiveness.

The Australian energy industry is undergoing significant change, affected by strong economic growth, population growth, micro-economic reform and environmental policies. However, against this background, policy needs to be set to maintain the reliable supply of competitively priced energy for business and individual needs as well as to minimise adverse impacts on the environment.

6. COMMENT ON KEY ISSUES RAISED BY GOVERNMENT

The Government discussion paper has raised several specific issues for public comment. These are:

6.1 Cost-effective Opportunities

What are the most cost-effective opportunities for reducing greenhouse emissions from energy supply and use in Victoria?

The most cost effective options for industry are the voluntary incentives that offer positive reinforcement to increasing the efficiency of plant and encouraging innovation in solutions to removing CO_2 from the atmosphere.

Continued Government support is required to ensure the new brown coal exploration licence holders are able to implement their plans and achieve the GHG emission targets they have agreed to.

The continued and increased financial commitment by Government to new coal technologies is the most effective long-term solution to achieving the aim of GHG abatement and continued economic prosperity in Victoria. Our dependence on coal and our abundant reserves require that we aggressively pursue the development of these new coal technologies.

Victoria is well placed to develop technology for geo-sequestration. The techniques developed will be heavily influenced by existing re-injection technology employed by Victorian gas producers. We would recommend that the government continue to investigate geo-sequestration opportunities to capitalise upon Victoria's existing know-how and favourable geology.

In addition, Government initiatives to improved demand side management by reducing the amount of energy, including electricity, gas and import-dependent transport fuels, consumed are a necessary and cost-effective component to any program to abate GHG.

6.2 Targets

What level of reduction in energy greenhouse gas emissions should be sought and over what time frame?

There already exists a broad national target and timetable for GHG emissions. The Commonwealth has a stated policy of achieving the Kyoto Protocol targets for Australia (although it is not intended to ratify the agreement). We believe that the Bracks Government should not impose any targets or timetables that are not consistent with an agreed national approach.

Industry broadly supports the 108 per cent Kyoto target objective but believes that this should be applied on a national basis without adversely impacting on Australian industry competitiveness. Applying pro rata requirements on States or industry sectors is both costly and ultimately counter-productive as seen by the NSW State based scheme.

6.3 Policies and Programs

What policies and programs should be considered to achieve reductions in energy-sector emissions while ensuring timely investment in new energy supplies and how the preferred policies might change over time?

The VMEC does not support the introduction of non-tradeable taxes or levies. Whilst such instruments send a signal to industry to reduce GHG they are very blunt greenhouse policy instruments and provide a negative incentive and place the financial gain with the Government and the costs ultimately on the consumers. We similarly do not support the introduction of tradable emissions permits as they are a market distortion.

Research undertaken by the minerals industry on the impact of a carbon tax or tradable emissions indicates that some key mineral processing businesses will

suffer considerable cost burdens. A modest US$10/t of CO_2 charge will increase the cost of processing alumina by 21%, and refining aluminium by 16%, magnesium by 16% and titanium metal by 7%. Such cost increases could readily make these businesses uneconomic in the global market, especially as the same metal produced in non-annex 1 countries will get a free carry on these cost penalties.

In addition, strategies of Government that aim to impose mandatory GHG emission targets on existing stationary energy plant and coal licences should be avoided entirely. It is noted that the State's energy producers are all privately owned and operated. Any alteration to existing licence conditions could result in adverse financial outcomes for existing investors, the Government, and future electricity consumers.

The Greenhouse Gas Acquisition Scheme (GGAS) is supported as a broad principle by industry and we recommend that the Victorian Government promote this approach to the Commonwealth.

The GGAS proposal involves the Commonwealth acquiring GHG emissions abatement through regular tender/bid rounds and includes mandatory Greenhouse Challenge participation. It has been developed as an alternative to other proposed market intervention instruments for GHG abatement – principally a carbon tax and/or domestic emissions trading.

GGAS is the only national proposal that:

1. will reduce emissions -
    a. without damaging the economy,
    b. without constraining growth,
    c. without eroding competitiveness,
    d. through least cost actions/projects,
    e. in an equitable manner – open to all sectors and does not impose unrecoverable costs;
2. will encourage investment in emissions abatement;
3. will be attractive to all sectors including agriculture/land use;
4. can be expanded if strong economic growth results in increased emissions;
5. can be adjusted to suit the size of the budget and the extent of emissions reduction required;
6. can operate for an extended period if conditions for efficient and equitable international emissions trading are slow to evolve;
7. can be wound up without creating sovereign risk concerns or expensive property rights which need to be "bought back" – and is therefore a low risk introduction to start the price formation process for emissions abatement; and
8. can transition to emissions trading at some future time without economic loss or sovereign risk concerns.

GGAS is an incentives-based market approach to GHG abatement which provides a solid base for building capacity in the economy to make the transition that would be required in a global, comprehensive GHG abatement system.

6.4 Government Role

Should government play any direct role, beyond its current commitments, to develop and demonstrate new energy technologies?

In addition to continued and increased direct involvement in R&D programs aimed at new technologies for all sources of energy the Government should consider incentives to industry that will bring the new technologies into production. These could include payroll tax incentives, licence fee reductions, and fast-track licence approvals for example.

6.5 Energy Markets

Are there shortcomings in the current operation of the energy markets that would need to be overcome to reduce emissions from the energy sector while providing for energy security?

The current national electricity market suffers from severe market distortions. For example, Victoria has the tightest supply scenario and yet the producers are receiving lower prices than the NSW and Queensland producers who operate in a market that have excess capacity. In addition, the Qld government continues to build new coal fired power stations in a market that is more than satisfied. Until the national market for electricity removes the distortions created by Government ownership of producers in other states we should not place additional burdens on the Victorian producers through the imposition of GHG abatement expenses. We believe that it is important to fix the market first.

6.6 Victoria's Competitiveness

What would be the implications for Victoria's competitiveness of taking further action to reduce emissions from the energy sector, and how could the potential impacts be mitigated?

The VMEC considers that we need a nationally consistent approach to GHG abatement measures. Any Victorian schemes should be consistent nationally. In addition, there should not be special arrangements that isolate sectors or consumers from the costs of imposing any national measures.

6.7 Bracks Government Initiatives

Are there particular policies and programs that the Bracks Government should consider for implementation irrespective of the outcomes of national processes?

The Bracks Government's approach to energy policy is fragmented over a number of agencies and Departments that diminish the ability of Government to management the diverse energy industry. The Government should improve coordination within the bureaucracy. Through this process it should also aim to ensure transparency in the development of energy policy.

Should the Bracks Government determine that it will implement some form of market intervention instrument on GHG emissions then great care is required to ensure that the aims of the strategy are actually achieved. Governments often have difficulty in effectively engaging in complex market systems. It may be better for the Government to consider commercialisation of the instruments to be implemented so that effective market behaviours are achieved for both the vendor and purchaser.

6.8 Other Issues

Respondents are invited to raise other relevant issues that may not appear on this list.

The VMEC considers that there is a need to ensure that any market intervention instruments cannot be manipulated to strand Victorian energy producers or create a distorted price for Victorian industry. Also, effective strategies are required to ensure that gaming of any tradable credits or hedging do not distort the aim of the credits to reduce GHG.

In addition, we believe that effective GHG accounting principles are required and measurement of emissions improved.

The Commonwealth's Greenhouse Challenge Program should continue to be supported by the Victorian Government and encouragement offered to broaden its application. The Program should operate as the single national system for monitoring and reporting inventories, abatement actions and levels of abatement. This would create the first basic step towards a national GHG emissions management scheme, namely:

- preparation of inventories and forecasts based on identification and measurement of emission sources and sinks;
- assessment of opportunities to take abatement action; and
- performance tracking and verification.

7. VMEC PREFERRED OPTIONS

The VMEC supports the goals of the Victorian Greenhouse Strategy and the Bracks Government commitment to reduce Victoria's GHG emissions whilst not placing the States economy at risk. Our members wish to assist in achieving the best environmental, social and economic outcome for Victoria.

We recommend that the Bracks Government hold any actions related to implementing market intervention instruments until the current Commonwealth review process is completed. It is important that we ensure a nationally coordinated approach rather than a fragmented State based system of abatement measures. After all, we should be smarter than our forebears when they developed our rail system.

Further, we believe that the nationally coordinated response should take a long-term perspective, maintain the competitiveness of Australian industry and share the burden of GHG abatement equitably across the community.

We do not support market intervention instruments that distort the energy market. In particular we do not support the introduction of non-tradable taxes or levies as they are a negative incentive and place the financial gain with the Government and the costs ultimately on the consumers. We similarly do not support the introduction of tradable emissions as they only serve to distort the energy market.

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The Greenhouse Gas Acquisition Scheme (GGAS) is supported as a broad principle by industry and we recommend that the Victorian Government promote this approach to the Commonwealth. The GGAS proposal has been developed as an alternative to other proposed market intervention instruments for GHG abatement which threaten the international competitiveness of key Australian industries. We support schemes that encourage energy producers to implement measures to reduce GHG through incentives.

We encourage the Government to continue and increase its support of R&D into new technologies that will enable the States world-class natural resources to be utilised. One of the most effective instruments for long-term solutions to GHG abatement is through the introduction of new technologies. The technology solution to climate change requires the support of Government and should include R&D into emission reduction and thermal efficiency improvement for thermal power plants as well as R&D for renewables.

The successful implementation of the new technologies is critical to Victoria continuing to benefit from the wonderful endowment of low sulphur, low ash (but high moisture) brown coal.

8. CONCLUSION

GHG abatement measures are a response to climate change concerns which are clearly an environmental issue, although solutions such as the Kyoto Protocol and its complex arrangement of instruments are political /economic instruments that have more to do with global trade and economic positioning than achieving desired environmental outcomes.

It is important that Victoria's response to climate change and GHG abatement continues to be considered as part of a broader Australian and global solution. The minerals industry supports the need for all parts of the Australian economy to make an equitable contribution to the international effort to reduce GHG emissions.

The minerals industry is committed to supporting a global response to managing climate change that will deliver real GHG emissions abatement, that does not undermine Australian industry's international competitiveness and creates real business opportunities.

Australia's greenhouse response should be coordinated at the national level, take a long-term perspective, maintain the competitiveness of Australian industry and share the burden of GHG abatement equitably across the community.

It is important that efforts to reduce GHG emissions do not harm Victoria's competitive power supply which underpins the industrial success of the State. This power supply is based on our endowment of a world-class brown coal resource. Brown coal is the fuel for 85 per cent of Victoria's electricity. We are blessed with huge brown coal resources in the Latrobe Valley with enough coal for 500 years at current demand levels. We need to develop the technology that will enable this wonderful natural endowment to be effectively utilised.

Any policy fundamentals of the Bracks Government should be aimed at attracting new generating capacity to Victoria. We have significant natural resources and these should be applied to the base load increases in generating capacity required for the future. Victoria should see itself proudly as the powerhouse for Australia.