



Alinta Submission

Alinta welcomes the opportunity to comment on the proposed National Greenhouse Gas Emissions Trading Scheme (NETS).

Alinta is a leading energy company with operations and investments that span Australia and New Zealand. Since listing on the Australian Stock Exchange in October 2000, Alinta has grown to become an ASX Top 100 company with a market capitalization approaching \$5 billion. Alinta manages, operates or owns a diversified portfolio of energy assets worth \$14 billion.

Alinta supports the principle that a market based response should form the core of any government response to restrict greenhouse emissions and believes the proposed NETS scheme design has many desirable features.

Alinta shares with the States and Territories the view that any emissions trading scheme must be national, including all States and Territories, and preferably should be lead by the Commonwealth. The NETS should not proceed in the absence of all States and Territories.

Comments on some the key aspects of the proposed design follow.

Nature of permits

Alinta supports the principle that permits must provide secure property rights.

When implementing an emissions trading scheme, governments must commit to paying fair compensation if they significantly change the rules of the scheme or targets in such a way as to reduce the value or security of permits.

Permit allocation

Alinta supports the use of a national approach based on auctioning as the most efficient method to allocate emissions permits.

We note and support the use of auctioning as the core allocation method in the NETS proposal. Allocating a smaller percentage of permits to existing generators to compensate for economic loss appears reasonable, although full auctioning with compensation paid separately out of the proceeds would seem simpler and warrants further investigation.

It is important that permits are allocated in an efficient and non-discriminatory manner, and that there is fair compensation for investments made in good faith under existing regulatory conditions. Full grandfathering should be avoided as it creates perverse outcomes, encourages gaming, discriminates against new investment and transfers wealth from the community to the largest or least efficient emitters of greenhouse gases – essentially paying the polluter.

Assistance measures

The definition of 'existing generator' for the purpose of calculating compensation should include any new projects that have commenced construction and/or committed significant resources to the development of their project before the proposed scheme is legislated.

Compensation should be based on individual power stations, not generating portfolios.

Potential investments are generally assessed on a stand alone basis; many are individually project financed and often have complex ownership structures. Determining compensation based on generating portfolios would be very complex and undesirable. Companies who have made investments in low or zero emission technologies have taken risks in doing so and may even have paid a premium in expectation of future carbon constraint. They should not be penalised by having the benefits of their early action removed by offsetting against other investments they may hold.

Further work is required to establish baselines for existing generators for the purpose of allocating free permits to make existing generators whole under the scheme. In particular, it will be necessary to establish a framework for calculating baselines for dual fuel facilities and facilities where significant changes to the configuration of the plant are made (e.g. conversion of peaking plant to CCGT or cogeneration) taking account of the impacts such changes have on both emission intensity and running hours. It is important that owners of generators where changes are already planned at the time when the scheme comes into force are not disadvantaged by the scheme.

Alinta supports the need to maintain the competitiveness of Australia's trade exposed, energy intensive industries. The proposal to link annual compensation to Australian production will help ensure the wider community benefits from any additional costs borne by the community to exclude this sector from the cost impacts of carbon trading. There should be ongoing assessment of the necessary levels of compensation for the trade exposed industries. For example, if similar schemes are imposed in countries competing with Australian trade exposed industries the level of compensation may need to be re-set or phased out altogether.

Coverage

The initial restriction of the scheme to large emitters is desirable to reduce the administrative burden. However, this restriction should be re-assessed if it becomes apparent that it creates distortions in the market, with a bias towards constructing less efficient, smaller 29.9MW generators.

Restricting the scheme to stationary energy is disappointing as it will reduce the ability of the scheme to produce least cost abatement; however we acknowledge the importance of ensuring emissions from a covered sector can be efficiently and accurately measured.

On this point, Alinta does not agree with the assertion in section 2.3.3 that fugitive emissions from gas transmission, and more particularly gas distribution, can be measured. At best they can be estimated with relatively low precision or accuracy. Prior to extending the scheme coverage to the gas transmission and distribution sectors, the government would need to work extensively with the industry, and the existing economic

regulators of these assets, to develop a robust, accurate methodology to estimate emissions and allocate liabilities through the gas supply chain.

The principle of compensating adversely affected assets must also apply to the natural gas sector and any other sector of the economy that the scheme may be expanded to cover. Although the natural gas industry may generally be expected to benefit from an emissions trading scheme, this will not be uniform and some assets may be adversely affected.

Penalty and make good provisions

The penalty should be set at a level to promote compliance and cap the cost of the scheme. To ensure the scheme cost is capped, there should be no make good provision.

Offsets

Offsets are critical to facilitating least cost emissions abatement, particularly when the coverage of the scheme is narrow and confined to one sector of the economy. Offsets should allow all other sectors of the economy with lower cost abatement opportunities to register and participate in the scheme.

Importantly, a robust but simple offset creation process provides an incentive for non-covered sectors to reduce emissions early.

In the absence of an effective offset mechanism, companies in non-covered sectors may delay low cost emission abatement opportunities in the expectation that when their sector is covered they will receive more compensation, and then implement the reduction project to reduce their liabilities.

All sectors and activities should be eligible to register for offsets, with the onus on the particular project to prove that the offset is genuine, additional and measurable.

To facilitate the process, standard rules should be developed for key areas, such as those identified in the discussion paper, but this should not exclude the possibility of projects in other areas.

Consideration should be given to allowing innovative new or trial offset approaches to generate certificates, backed by financial bonds that would ensure permits could be purchased to make up a shortfall if the offset project did not deliver all the expected benefits. This would allow risk to be shared and may bring forward innovative solutions that might otherwise take years to prove the quantum of abatement delivered.

Creation of certificates from offsets should coincide with the period in which the abatement is delivered; for example, abatement delivered in 2015 should not be able to be used as an offset for a 2010 emission.

Provided that the offsets represent genuine additional emissions reductions, there is no environmental difference where the reductions come from and so there should be no limit on the number of offset permits that can be generated.

Institutional Arrangements

Alinta supports the use of the existing energy market regulators.

If it becomes apparent that the NETS scheme will be implemented, the Commonwealth should consider cooperating to allow the use of existing bodies, and to simplify the legislative process (ensuring national consistency) – even if it disagrees with the scheme in principle.

Emissions monitoring, reporting and verification

We agree in principle that monitoring and reporting should be based on the proposed streamlined national process being developed for the Council of Australian Governments (CoAG).

However, the preferred option identified for that program is for company level reporting based on operational control. Mandating reporting based on operational control seems fundamentally inconsistent with the needs of an emissions trading scheme where real wealth is created and distributed through secure, tradeable property rights to emit carbon. Monitoring, reporting and verification for an emissions trading scheme must be tied to liability under the scheme and ownership of permits – that is ownership and/or financial interest, not operational control. Also, consolidation to related entities will be irrelevant as it is facilities that are liable under the scheme.

A national response to greenhouse abatement should also seek to replace and/or harmonise all other greenhouse related programs which apply to the scheme participants.

Other regulatory measures

The NETS design identifies that it would be possible for the scheme to operate in parallel with various other state and national schemes, however this undermines the benefits of a consistent national approach. If complementary mechanisms to support renewable energy, and/or zero emission technology are required, then these should also be national and designed to harmonise administration with the core emissions trading scheme as far as practical. Appropriate compensation should be provided where investments under existing schemes are adversely affected through this consolidation, in order to avoid creating sovereign risk.

Most importantly, existing and proposed regulatory responses that mandate particular technologies and/or emissions intensities for plant in covered sectors should be scrapped. Such schemes are inefficient, burdensome and frequently result in perverse incentives and outcomes. It is important to note that the scheme cap will determine the overall level of emissions from a covered sector, additional regulations only change allocation of emissions with the sector – the very job that an emissions trading scheme is set up to do.

For example, Western Australia's greenhouse strategy requires 'best practice' greenhouse emissions for new electricity generators. AlintaAGL is currently building a new gas fired generator at Wagerup which will initially be operated as a dual fuel peaking plant prior to conversion to cogeneration when sufficient demand exists. The plant will be considered best practice by the EPA when operating as a peaking facility and when converted to cogeneration. However, as demand increases beyond what is considered peaking, but before it is sufficient to support conversion to cogeneration, it will not be considered best practice and will be required to purchase greenhouse offsets. At all times, when running on gas, the plant will generate electricity with significantly lower greenhouse intensity

than the WA grid average and best practise coal generation. The effect of this regulation which is intended to minimise greenhouse gas emissions will increase the costs of a low greenhouse intensity generator, reducing dispatch from the plant, and effectively subsidise increased generation from higher greenhouse intensity plant.

If requirements like those described above remain in place, they serve to negate some of the desirable effects of an emissions trading scheme which would otherwise tend to encourage lower greenhouse intensity generators. By increasing the operating cost of the new low intensity generator, it would allow an existing higher intensity plant to profitably pay more for emissions permits.

Alinta's design principles for greenhouse abatement policy

In addition to our comments above, we have included the policy principles that Alinta has adopted to guide our response to greenhouse policy.

Greenhouse policy ought:

- Be national, transparent, integrated and comprehensive;
 - *The policy should consolidate the current mix of policy measures into a rational comprehensive policy response.*
 - *The policy mix will likely need to include support for R&D and industry development, but the core should be a market based carbon price;*
- Be market based, non-discriminatory and have clear long-term targets;
 - *Markets should decide the optimal mix of energy sources and technologies. New entrants must not be discriminated against.*
 - *Industry development programs (eg for renewable energy or zero emissions technology) should be broad and market based, leaving the market to determine the best mix of technologies to pursue with the program.*
- Be explicitly linked to energy market regulation;
- Promote least cost, growth stimulatory, to the economy;
- Equitably distribute burden sharing, including full pass through of costs to the end user where appropriate;
- Protect trade exposed energy intensive sectors of the economy; and
- Have low administrative costs to participants.

Further, design of emissions trading schemes ought to:

- Allocate permits in a manner that is economically rational;
 - *By auction or production intensity, not historical performance (or grandfathering).*
 - *Permit allocation must not discriminate against new entrants.*
- Cover all industrial sectors to ensure the broadest market, but limit mandatory coverage to large emitters and the main greenhouse gases;
- Be revenue neutral; and
- Be broadly compatible with international instruments, without compromising the efficiency of Australia's solution.