GRIFFIN ENERGY

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The Secretary
Senate Select Committee on Climate Policy
Department of the Senate
PO Box 6100
Parliament House
Canberra ACT 2600

Dear Committee Secretary,

RE: Submission to inquiry into policies relating to climate change.

Griffin Energy welcomes the opportunity to make a submission to your inquiry. Our submission, and interest in the inquiry, focuses on the terms of reference specific to investigating the implementation of an emissions trading scheme as the central policy lever to reduce Australia's carbon emissions.

Background to Griffin Energy

Griffin Energy, part of the diversified Griffin Group of companies, was established with a view to providing a secure and reliable source of electricity into the Western Australian market. This was a direct response to recent reforms in the WA electricity generation and supply markets aimed at encouraging private generation investment and retail entry. Griffin Energy is developing a balanced portfolio of generation assets within the isolated WA market. Production of electricity has recently commenced from the first of 2 x 229MW (gross) coal fired units at the Bluewaters Power Station in Collie. In joint venture with the Stanwell Corporation, Griffin operates an 80MW wind farm near Cervantes. Other generation developments include: the scheduled expansion of the Bluewaters Power Station; a proposed gas fired power station north of Perth; as well as further renewable energy developments including a second wind farm (coupled to a wind following peaker) and innovative wave power and hydro technologies.

General comments on the proposed CPRS design

The Griffin Group has consistently supported the concept of introducing an Australian Emissions Trading Scheme as part of an international effort to price the externalities brought about through the emission of greenhouse gases (GHG) from otherwise productive industry. We have maintained that such a scheme should be broad based where practicable; offer a high level of certainty to investors; and strike an appropriate balance between the benefit of

Australia's likely contribution to the global emissions reduction effort and the potential disruption to Australia's relatively emissions intensive economy.

With diverse business activities across a range of sectors impacted by the CPRS, including agriculture, coal mining and our electricity generation investments, Griffin maintains a keen interest in the development of policy in this area. While Griffin has consistently supported the concept of an Australian Emissions Trading Scheme, we are equally adamant that the design and implementation of the scheme should be robust and uncompromised. Importantly, it must be understood that transitioning away from a carbon intensive economy takes time. While we firmly believe that, over time and given the appropriate incentives, innovation will move Australia from a relatively high to a low carbon economy, the scheme design in the interim period must give regard to the physical and financial constraints in implementing low emission technologies during this period. Griffin believes that at all times, the integrity of the scheme and the best interests of Australia should be the priorities when making policy decisions on appropriate responses to climate change.

Emissions trading as a central policy lever for reducing climate change

An emissions trading scheme is a market based mechanism. Private capital is employed to deliver returns within the new parameters set by the scheme design. Most economists would suggest that this principle leads to greater efficiency than would otherwise be achieved through the use of public funds (taxation) by governments to achieve a similar outcome. Experience of governments 'picking winners' has a chequered history. Private finance's requirement for equity returns will theoretically drive innovation, which will lead to a faster implementation of new technologies; and an investment discipline that will seek out the lowest cost investments and abatement. However markets are dynamic and complex environments. Altering the parameters of an existing market will have profound effects on the existing operators in that market. In the case of emissions trading, the assumption that the market will move seamlessly from a high emissions state to a low emissions state is incongruous with reality. This is a real-world criticism of the theoretical economist's market based approach; however it is not an excuse to abandon such mechanisms. Careful design of the implementation of an emissions trading scheme can overcome many of the issues confronted in the transition from the existing market paradigm to the new.

The most important implementation philosophy is around timing. Investments in the emission intensive economy tend to be large, lumpy and long lived. This is very different to other sectors of the economy, such as the IT sector or services sectors, where businesses are less capital intensive and more flexible to frequent evolution. The long lead times required to transition away from an emission intensive economy may be difficult to reconcile with the perceived urgency of the task. However, inadequately addressing this design issue may lead to significant dislocation within markets resulting in large and volatile impacts on the general economy. This is reasonably well understood in the EITE sectors, where carbon leakage is neither commercially or environmentally beneficial. While there has been considerable effort expended in designing a scheme to mitigate these effects, the complexity of implementing solutions suggests that more detailed analysis and planning is required. A poorly designed system implemented prematurely will not produce the most efficient outcomes.

A less well understood sector in which significant transitional upheaval will take place within an existing nuanced market, charaterised by very capital intensive and long lived investments, is the electricity generation sector. The principal pillar of the Government's Electricity Sector Adjustment Scheme (ESAS), which aims to mitigate the effects of imposing new parameters

on this exiting market, is that of direct transitional assistance to eligible coal fired generators. The rationale for assistance stems from the enormous amount of capital required to be invested into the Australian stationary energy sector over the coming decades; and at mitigating the perception of regulatory risk attached to the attraction of this capital. By applying a layer of regulatory risk to this investment challenge, where current equity investors face significant write downs to investments; and even some debt providers face the prospect of unprecedented losses to principle[1], attracting the requisite capital to meet the energy investment challenge of the carbon constrained world will not only be difficult, but likely to attract a considerable additional risk premium than would otherwise be the case. This builds an artificial inefficiency into the market based mechanisms of emissions trading. A way to mitigate the perception of regulatory risk, through scheme design, is to compensate generators that suffer significant losses attributable to the new market parameters. This shows that while governments may be inclined to undertake bold and far reaching economic reform, it does not do so at the expense of capital providers that have, in good faith and under a different market paradigm, invested in growing the capital stock of Australia's electricity industry and the productive capacity of the nation[2]. Such a design mechanism needs to accurately reflect the losses to asset value attributable to the new parameters imposed on the existing market. Importantly, it also needs to reflect the long lead times required to transition the market from a state where it operated effectively under the old paradigm, to the new. This transition will require significant investment in new technology – technology not yet in existence in many circumstances – as well as the competitive relationships between the outputs of new and existing technologies to coalesce into a functioning marketplace that is universally recognised for its complexity[3]. If the detailed design of a market based emissions trading scheme does not account for the long lead times required for transitioning to a low emission electricity sector, it risks imposing significant dislocation to the electricity market which will likely lead to volatile and inefficient costs being imposed on the larger economy.

Griffin has been an active participant in the robust consultation process that has been undertaken to date in this area. We have a significant stake in ensuring that the implementation of climate change policy leads to efficient outcomes that are in the best interests of Australia. We intend to continue to be actively involved in further consultation between government and industry.

Yours sincerely

Shane Cremin
GM – Policy & Strategy

[1] See 'Emissions trading, toxic debt and the Australian power market', Simshauser, 2008
[2] The Australian economy has benefitted greatly from a reliable supply of low cost electricity.
[3] The inability to store electricity (i.e. its instantaneous production and consumption) sets it aside from other commodity markets.