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14 November 2012

Climate Change Authority
GPO Box 1944
Melbourne VIC 3001

By email: enquiries@climatechangeauthority.gov.au

Dear Sir/Madam,

AGL Energy Response to the Climate Change Authority's Renewable Energy Target Review Discussion Paper

AGL Energy (**AGL**) welcomes the opportunity to provide feedback on the Renewable Energy Target (**RET**) Review Discussion Paper (**Discussion Paper**) issued by the Climate Change Authority (**CCA**).

AGL supports the direction taken by the CCA, particularly its decision not to make major changes to current policy settings in the interests of ensuring policy stability and predictability. AGL is especially supportive of the CCA's draft recommendation to retain existing LRET targets, to retain the separation of the LRET from the SRES, and to reduce the regularity of scheduled reviews of the RET scheme from two yearly to four yearly.

However, we wish to highlight two particular issues that require the CCA's attention:

Importance of economically-sound retail electricity pricing principles to support achievement of the RET

The CCA would be aware of AGL's recent public statements expressing concern that sub-optimal regulatory pricing decisions in Queensland and South Australia would be likely to have a detrimental impact on investment in renewable energy generation. To be clear, AGL believes that achievement of the RET is possible, provided sensible and economically efficient pricing decisions are made by jurisdictional pricing regulators. Fundamentally, the setting of retail price caps below the long run marginal cost of supply inhibits retailers', such as AGL's, ability to recover the cost of their investments in new generation capacity.

The deregulation of retail electricity prices and removal of retail price caps is in the long term interests of the electricity industry and consumers by incentivising efficient investment in electricity generation (including the renewable energy generation necessary to meet RET targets), and promoting competition in retail electricity markets. It is important that the CCA draws the attention of policymakers to this causal relationship, and strongly recommends to State regulators the need for retail electricity price deregulation where competition is effective.

At a minimum, where price regulation is retained the CCA should advocate that default tariffs be set to reflect the long run sustainable cost of supply (ie. with long run marginal cost as a floor) to ensure that any price cap is not incompatible with the proper functioning of the market (ie. to facilitate competition, innovation and new investment). Where regulated prices do not reflect long run sustainable costs, it impacts on retailers' ability to invest in new generation, hence stifling new plant entry into the NEM, raising the cost of capital, and potentially threatening the likelihood of meeting RET targets, and security of energy supply more broadly.

It is particularly important that the RET not be changed in an attempt to accommodate for or to correct inefficient or sub-optimal jurisdictional pricing decisions. This would lead to perverse outcomes that would in fact further exacerbate the policy uncertainty that currently exists around carbon pricing and climate change policies, and would risk the achievement of RET targets irrespective of their level. Instead, the CCA should emphasise to governments at federal and State levels the need for pricing methodologies that support an economic environment conducive to meeting RET targets (and investment generally).

Delay consideration of the proposed removal of the exemption for self-generators until 2016 review

The CCA proposes to remove the exemption from RET liability for new self-generation on the grounds that there is no strong case for this exemption to exist particularly given that the carbon price will encourage less emissions-intensive self-generation where it is cost-effective to do so.

The considerable uncertainty that currently exists around the future of the carbon price discourages significant investment in and the development of low emissions-intensive energy generation. With this uncertainty largely muting the price signal that the carbon price would otherwise create, cost-effective, low emissions-intensive self-generation is strongly incentivised by the exemption from RET liability that currently exists.

AGL considers it to be premature to remove the exemption for self-generation at this stage, and suggests that the CCA revisits this issue in its next review of the RET scheme scheduled for 2016. By this time we would expect there to be greater certainty as to carbon pricing policy settings, which would enable the reasoned determination of whether there is a need for additional incentives for low-emissions self-generation.

In any case, AGL is strongly in favour of the retention of the exemption for existing self-generation projects. The costings for these investments rely on the existence of the exemption, and removing it would significantly increase their cost structures in such a way as to threaten their economic viability.

We would be happy to discuss any of these issues with the CCA if this would be helpful. Please contact me on (02) 9921 2516 or tanelson@agl.com.au or Anita George at ageorge@agl.com.au or on (03) 8633 7212 if you would like to discuss AGL's views.

Yours sincerely,

Tim Nelson
Head of Economic Policy and Sustainability