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## Abbott government's energy white paper fails to face reality

By failing to take global warming seriously, the white paper discourages solar power, encourages doomed coal investment, hobbles the RET, and misses the chance to raise petrol taxes.



Competition from decentralised power is challenging the market position of established suppliers. *Bloomberg*

by **Ross Garnaut**

The federal government's white paper on energy contains the good, the bad and the ugly.

The good is the focus on effective competition as an agent of productivity growth. Regrettably, good statements in principle are not followed through into policy positions.

The bad is the failure to face up to big problems in the economy that are affected by the resources sector.

The ugly is failure to face up to the reality of climate change.

The white paper converts sound principle into good practice in opposing payments for closure to power generators. Three-quarters of Australia's coal-based generators are living beyond their design dates. Those that are losing money need no help to close.

"Cost-reflective pricing" within a competitive market is desirable. But what is cost-reflective pricing within a natural monopoly?

Competition from decentralised power is challenging the market position of established suppliers. The white paper wants to block the new competition, by requiring owners of solar PV to pay for access to the grid through higher fixed charges. There is a place for a fixed component of network charges to reflect the costs of maintaining the network. Cost-reflective pricing would charge for economically valuable peak capacity – not fixed charges that are independent of peak use, nor to cover network investment errors from 2006 (not 2010, as asserted by the white paper).

### **No benefit**

The white paper is against cross-subsidies to owners of solar PV systems, but not the much larger ones from urban to regional and from household and small business to large business users. The urban-regional transfers convey no benefit to many intended beneficiaries now that many can meet their own requirements locally at lower costs to themselves. The unintended consequence of applying fixed charges indiscriminately is uneconomically large incentives to disconnect from the grid.

The white paper notes Australia's relatively rich endowment of renewable energy resources. It fails to point out that this can be a permanent source of lower domestic energy costs within a free-trade policy. By contrast, lower domestic costs from fossil fuels are corroded by export parity pricing.

The bad is to see Australia's energy future principally in terms of exports of fossil fuels and indiscriminately low domestic energy costs.

The white paper uses the International Energy Agency's "New Policies" scenarios to encourage expanded exports of fossil fuels from Australia. "New Policies" reflects policies announced some time ago. The IEA says that this scenario is unsustainable because it is likely to lead to an intolerable increase in world temperatures. Nor does the paper recognise that these projections of Chinese and global demand for coal are already obsolete. This obsolescence means that tens of billions of dollars of investment in expanding coal supply capacity will never return the cost of capital. A better-informed government might have encouraged caution into private decisions, instead of reinforcing errors.

### **Large budget problem**

You would not know it from the white paper, but Australia has a large budget problem. Taxes on energy, resource rents and pricing of environmental costs could make a large contribution to solving the budget problem at low or no economic cost. The white paper takes pride in Australian petroleum fuel prices being at the lower end of the Organisation for Economic Co-operation and Development range and in the recent abolition of the carbon and mining taxes.

New Zealand is held up as a model of higher indirect and lower direct taxes. Australia could raise petroleum fuel taxes by 25¢ a litre and still have substantially lower prices than New Zealand, lower prices than Australians were paying less than a year ago, and lower prices than most of the OECD. Without exemptions, that would raise as much revenue as an increase by one quarter in the GST. Unlike an increase in the GST, it would not require the agreement of all states. The proceeds could go to the states on a per capita basis. The energy efficiency and climate change gains would be a bonus. Surely the Greens and the Labor Party in the Senate have learned from the rejection of restoration of excise indexation.

Economist Max Corden, in a recent article, explained that restoration of carbon pricing would make a substantial contribution to the revenue at low economic cost. The Henry Tax Review placed efficient resource taxation at the top of its list for raising revenue at low cost.

Finally, the ugly. The white paper does not take climate change seriously, and yet the global energy story interacts everywhere with concerns for climate change.

The white paper notes the importance of carbon capture and storage to the future of coal. It does not mention that carbon capture and storage will never be deployed without regulation or a carbon price.

The white paper does not discuss the emissions controls that are necessary for an emissions reduction fund to be effective. It therefore avoids the contradiction between support for competitive markets and abolition of carbon pricing.

The white paper disparages the Renewable Energy Target (RET), while arguing for a 20 per cent target. My Climate Change Review preferred carbon pricing to the RET. This preference is supported by the Warburton committee, which uses the superiority of carbon pricing over a mandatory target to argue for abolition of the RET.

## Context changes

The whole context changes without carbon pricing. Analysis, including the modelling undertaken for Warburton, shows that the RET substantially reduces carbon emissions in the electricity sector while reducing the present value of electricity costs for users. Keeping the RET target at 41 Twh would reduce electricity costs. Some coal-based electricity generators would face earlier closure. Temporary underperformance against the target would generate some government revenue with no damage to the economy and little upward pressure on prices compared with a lower RET target. Do the sums.

The white paper supports exemption of trade-exposed emissions intensive industry from RET obligations. The RET lowers wholesale electricity prices for emissions-intensive industries, which are already compensated for most of their renewable energy certificate obligations. With their losses already mostly socialised and their gains from lower wholesale prices capitalised, the white paper wants to increase the net subsidy.

The Age of Entitlement has never had it so good.

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