

**International Power's Application to
Develop Coal Resources Adjacent to its
Current Lease**

A Submission to Panels Victoria

by

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17 June 2004

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Summary

The Hazelwood Power Station is one of four key baseload electricity generators operating in Victoria. Considered almost obsolete at the time of its sale in 1997, it has been refurbished and transformed into a productive and reliable asset and its life has been extended 25 years beyond its previously scheduled 2005 decommissioning date.

The Minister and his colleagues within the Government have rightly promoted the need for integrity and an absence of political interference in approval processes. Moreover, the Government has been careful to prevent regulatory policies being used inappropriately for matters to which they were never intended to apply. The Minister, in line with such a philosophy, moved to prevent legislation designed to have only an interim effect on the electricity supply industry's structure from being used to prevent a takeover in the AGL - Loy Yang Power case.

The environmental approval processes for the development of the West Field Project are analogous to that case. Their focus is on ensuring appropriate local safeguards rather than addressing matters of global importance like greenhouse gas emissions. Misusing those local safeguard processes to pursue wider agenda issues would transform them into addressing goals that they were never intended to tackle.

In addition, the environmental approval process for specific project proposals employs a command-and-control regulatory approach. While necessary for specific project assessments, this approach is at variance with the preferred approach of governments, including the Victorian Government, for addressing environmental "spillovers", especially greenhouse gas emissions. The preferred approach for these national and global issues is one that employs "economic instruments", like taxes or tradeable rights, to pursue the objective since these market-based approaches have acknowledged superiorities in terms of efficiently meeting the goal.

Moreover, the Victorian Government has taken the view that the control of greenhouse gas emissions is a national policy and one for the Commonwealth to take the lead on. For Victoria to move ahead of the national program could disadvantage the State and distort the national approach.

The EES assessment will be seen by energy investors as a guide to Victorian's attitude to investment in brown coal powered generation. The West Field project is necessary for the on-going production of the existing Hazelwood facility. It is being deliberated at a time when, according to the electricity market manager (NEMMCO), not only is the existing facility important for the State and the national supply, but an additional major baseload facility will be necessary in Victoria within four years.

Finally, as a \$2.3 billion asset, the Hazelwood plant is among the most important investments in Victoria. The Panel's approach of the West Field project is, therefore, a litmus test of Victoria's the environmental assessment procedures with ramifications for investor confidence in regulatory process for investment plans across the State. .

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Introduction

International Power's 1,600 MW Hazelwood facility is responsible for some 20 per cent of the electricity production of Victoria and about 5 per cent of the output of the National Electricity Market.

The generator has undergone a remarkable upgrade since having been sold to its present owners for \$2.3 billion in 1997. It has been refurbished and thereby had its life extended by some 25 years, an outstanding example of efficient use of capital. In the process, the business has also reduced its plant downtime thereby improving the reliability and value of the electricity supply.

These improvements now need to be consolidated. To effect this, a modification of the business's mining licence (the West Field Project) is required along the lines that were agreed in principle at the time of the government's sale of the facility. That agreement was contingent on assurances that an Environment Effects Statement (EES) would be prepared and would conform to government policies for the protection of the environment.

The review of the process has some considerable implications including:

- the availability of low cost electricity in Victoria
- the integrity of Victorian Government environmental assessment procedures and the consequent credibility of the Government in dealing with business proposals

Scope of the EES

An EES is required to meet the requirements of:

- i) Victoria's *Environment Effects Act* 1978; and
- ii) environmental assessment requirements under the Commonwealth's *Environment Protection and Biodiversity Conservation Act* (EPBC) 1999.

Reflecting the regrettable build up of regulatory impediments to business, the coverage of the EES is required to be extensive, costly and the business planning is vulnerable to considerable area of potential administrative discretion. The EES is primarily subject to four Victorian Acts:

- *Mineral Resources and Development Act* 1990,
- *Water Act* 1989,
- *Environment Protection Act* 1970, and
- *Planning and Environment Act* 1987.

Other legislation and regulatory matters to be taken into consideration include:

- relevant State environment protection policies and Waste Management Policies
- *Latrobe Planning Scheme*

- *Catchment and Land Protection Act 1994*
- *Land Act 1958*
- *Crown Land (Reserves) Act 1978*
- *Archaeological and Aboriginal Relics Preservation Act 1972*
- *Flora and Fauna Guarantee Act 1988* and Victoria's *Biodiversity Strategy (Native Vegetation Framework)*
- *Heritage Act 1995* and relevant strategies and policies, and
- *Aboriginal and Torres Strait Islanders Heritage Protection Act 1984* (Commonwealth)

Assessment Guidelines were prepared by the Department of Sustainability and Environment (DSE) and Hazelwood's EES follows these.

Under the guidelines the EES must assess the potential environmental, social and economic impacts of the West Field Project and describe how the impacts are to be avoided or managed. They deal with a number of issues largely of a local character. These include river diversions and associated ecological impacts, road realignments, air quality due to the diversions.

A Works Approval under the *Environment Protection Act 1970* needs to address discharges of water and dust, and waste minimisation for the proposed works.

Greenhouse gas emissions are also covered. However, this issue had only a cursory coverage in the Departmental Assessment Guidelines. Indeed, out of some 800 pages assembled by International Power in response to the regulatory approval requirements and the Government's Guidelines only 7 (10.91-10.98) address greenhouse gas emissions as their prime topic, although the matter is covered alongside a great many other issues elsewhere in the report. Moreover, in line with the requirements of the EES, that section in Chapter 10, quite properly, dealt only with the proposed mining operations and not the subsequent burning of coal itself. This reflects the intent of the legislation to focus on the particular and not to provide a tool which the executive or regulatory arms of government could employ to pursue wide policy agendas.

It is understood that Hazelwood, as a separate matter, has provided assurances that greenhouse gas emissions per unit of electricity generated will decline as a result of the efficiencies in operation it intends to introduce. There are technologies for the geosequestration of CO₂ being considered, including one in the US that is being trialled with brown coal but even an Integrated Gasification Combined Cycle (IGCC) with geosequestration would only reduce the CO₂ emission levels to about 40 per cent or existing levels¹.

The Economic Effects of Rejecting the Application

A decision to prevent Hazelwood proceeding on the grounds that its greenhouse gas emissions are inconsistent with the state's policies and would deter additional

¹ See Iain MacGill, Hugh Outhred and Rob Passey, *The Australian Electricity Industry and Climate Change: What role for geosequestration?* ERGO Draft Discussion Paper 0503, October 2003. http://www.ergo.ee.unsw.edu.au/ergo_roleofgeosequestration_macgill.pdf

investment in brown coal based electricity generation. International Power maintains that it would not be possible to continue operating the Hazelwood plant as a commercial entity if access to the West Field is denied.

The National Electricity Market (NEM) now comprises generators, network businesses and retailers that are fully privatised (in Victoria and South Australia) and largely state owned in the other states. The state owned firms operate at arms length from their government shareholder under a corporatised governance model. Replacing the five integrated electricity businesses that were operating in the NEM ten years ago are about 30 firms, including over a dozen major generating businesses.

New capacity is commissioned and existing capacity operated solely on the basis of the ability of the firms to operate profitably.

The early decommissioning of the Hazelwood facility would leave a major shortfall in the State's capacity since the station provides more than one fifth of the state's electricity. This would be compounded because the steady growth in demand will require further capacity (by 2008 according to the advice of the national market manager, NEMMCO, in its Statement of Opportunities).

Alternatives using gas would be much more expensive while wind and other exotic renewables cannot possibly provide anything more than token quantities of electricity at a cost acceptable to Victoria. With respect to the more exotic renewables, (as defined by the Commonwealth) the requirement first made in 1997 by the Prime Minister in his response to the Kyoto Agreement that the Electricity Supply Industry requires 9,500 GWh per annum in terms of "additional energy" to be used across Australia. This will bring a cost of \$380 million per year by 2010.

The Prime Minister in his *Securing Australia's Energy Future* address (15 June 2004) estimated that this measure will have underpinned some \$2 billion in investment by 2010. In that address, further inducements the development of renewable energy were announced. For example, the Commonwealth's commitment of a \$500 million fund is designed to leverage a further \$1 billion of investment in these energy technologies, and there are further measures (including \$75 million for "solar cities", \$100 million for R&D).

Minister Theophanous has committed Victoria to the installation of some 1000 MW of wind power by 2006, though wind power can only provide about one quarter of the output of comparable fossil fuelled generators because of the intermittent nature of the wind.

The Prime Minister's 15 June 2004 energy address also estimated that between now and 2020 some \$37 billion in investment for electricity will be required. Most of this will be in the generation sector and little of it can come from wind. The Government doubtless regards it as important that Victoria continues to obtain a reasonable share (30 per cent or so) of this new investment.

Brown coal, in the absence of an improbable technological advance, is always likely to entail considerably greater emissions of carbon dioxide per kWh of electricity than

gas or black coal based generators. Only nuclear is capable of near zero emissions and nuclear is not favoured on other grounds.

That aside, the early forced decommissioning of Hazelwood would have additional repercussions for industry development in the State. These would be include:

- creating an adverse image for the State as a venue for major investment, compounding some unfavourable publicity as a result of industrial relations weaknesses that have already had an effect seen with the failure of the State to hold the mooted investment by Japanese food group Saizeriya and to attract the Barry Callebaut company and loss of other transnational investment²; Victoria's poor labour relations were further highlighted in the findings of the Cole Royal Commission;
- bringing about a wasteful scrapping of a major plant and signalling that the Government sees little merit in the further development of the State's extraordinarily rich deposits of brown coal;
- raising the costs of energy in the State with consequent losses in its ability to attract industry, especially energy intensive industry, and in bringing about higher energy costs to consumers;
- further costs increases in terms of transmission lines as a result of the need to import energy from NSW to make up shortfalls within the State.

Policy and Administrative Considerations

It has been said (Courier-Mail 10 May 2004) that, "A spokesman for the Energy and Resources Minister Theo Theophanous said the minister would not sign off on the mining licence expansion until negotiations with Hazelwood over a reduction in greenhouse emissions had concluded". It is most unlikely that such a report, if accurate, truly represented the views of the Minister.

One reason for this is because of the acknowledged importance of brown coal as a present and future energy source in Victoria. Minister Theophanous and the Victorian Government as a whole is strongly supportive of making full use of the States brown coal resources. At the Energy Users Association on the 2nd of June 2004 Mr Theophanous confirmed the Government's view of the vital importance to Victoria of these reserves. He said, "Brown coal will play a key role in meeting our future energy needs. But will do so within a carbon constrained environment".

The Government is also conscious of the need to provide a supportive and hospitable environment for investment in general, recognising its importance to the State's continued prosperity.

In addition to these industry specific matters, Mr Theophanous has been at pains to promote the integrity of government actions. These include ensuring due process in matters where government assessment procedures have been put in place and thereby avoiding political interference in specific matters. Mr Theophanous has emphasised the need for governments to adopt policy positions and ensure legislation is in place to promote these rather than interfering in particular commercial decisions.

² <http://ipa.org.au/pubs/workreform/foodfs.html>

In this respect the Minister is on-record as having denied the ACCC use of particular Victorian legislation to oppose the proposed merger between Loy Yang Power and AGL. When the ACCC sought to use the legislation of the previous Victorian Government for purposes it was clearly not intended, the Minister moved to rescind that legislation. This action, quite properly, forced the ACCC to pursue its policies through the medium of its own Act and not through Victoria-specific legislation that was targeted at matters other than those in dispute. It endorsed major tenets of sound administration, for example:

- that a single policy instrument should not be used to serve more than one unrelated policy goal; and
- that regulatory laws should be confined to purposes that represented the intent of the legislature at the time of their promulgation and should not provide a licence to the executive and regulatory branches of government to address unrelated matters.

Furthermore, the Minister, though strongly in favour of the Kyoto Agreement and in favour of doubling the current Mandatory Renewable Energy Target (MRET), made it clear when addressing the Energy Users Association on the 2nd of June 2004 that this was a national issue and it was quite improper for State Governments to attempt to pursue the policy individually. If Victoria were to adopt state-particular policies this might disadvantage the state's economy; it might also undermine the national approach by shifting it in directions that are not appropriate and more costly than they need be.

Moreover, both the Commonwealth and State Governments (and indeed, virtually all governments the world-over) are in agreement that any control mechanism used for greenhouse gas emissions should employ "economic instruments" like taxes, incentives or tradeable rights. These are superior to command-and-control regulations or direct prohibitions that are necessarily used in local planning decisions because they employ markets with the intrinsic improvements in flexibility this entails. MRET and the additional mechanism employed by the NSW Government make use of the economic instruments approach. For the Victorian Government, among other members of Cabinet, the Deputy Premier and Minister for the Environment has made a strong case for using market instruments to pursue environmental goals³.

For all these reasons, and in view of the efforts International Power has made to provide an accurate and informative EES that demonstrates the benefits of its proposed new investment to the State and the mitigatory actions it is taking to minimise any adverse environmental outcomes, the Panel should accept the proposal.

³ See address to the Fabian Society, RMIT May 2003, http://www.fabian.org.au/library/event_papers/1080393121_16398.html