The Policy Pitch - Climate policy in 2016: The hard task of delivering on our international commitment - Melbourne 16 February 2016

In the lead-up to December’s Paris climate change conference, the Australian Government committed to the target of reducing greenhouse gas emissions by 26-28 per cent below 2005 levels by 2030. But how will we get there? Much is at stake. Shayleen Thompson, CEO of the Climate Change Authority and Clare Savage from the Business Council of Australia joined Grattan Institute's Tony Wood to examine the issues: How tough is the target and what are the merits of the various policies that might be used to meet this and future targets?

Speakers: 
Tony Wood, Grattan Institute
Shayleen Thompson, Climate Change Authority
Clare Savage, Business Council of Australia

SARAH SLADE: My name is Sarah Slade and I’m Head of Storage & Digital Collection Services here at the State Library. It gives me great pleasure to welcome you all to The Policy Pitch. Tonight’s topic, as you’re aware, is Climate policy in 2016: The hard task of delivering on our international commitment. This seminar is held on the traditional lands of the Kulin nation and I wish to acknowledge them as the traditional owners. I’d like to give a warm welcome to tonight’s speakers, Tony Wood, Shayleen Thompson and Clare Savage. I’d also like to welcome Grattan Institute members and staff, and Friends of the Library. It’s very satisfying to see so many here this evening.

The Policy Pitch is a joint initiative of State Library of Victoria and the Grattan Institute. This partnership contributes to one of the Library’s major aims, which is to be a catalyst for ideas, discussion and debate. The series includes the brightest minds in the field of public policy and brings to the library a highly engaged and well-informed audience. It creates a space for in-depth discussion and reflection on important policy issues and this is one of a broad range of programs offered by the State Library and our partners. If you’d like to know more I’d encourage you to pick up our autumn What’s On brochure or have a look at our website to keep abreast of our free community programs.

I’d also encourage you to join our Friends of the Library, if you’re not already a Friend, and if you’re interested in this please pick up one of our foundation brochures, which is available in the foyer.

So in October last year we heard from experts in the field of climate change who discussed their views prior to the then upcoming Paris Conference last December and Tony, Shayleen and Clare, I’m looking forward to hearing your observations post-Paris about Australia’s climate policy options. I’m pleased to now introduced Tony Wood, who will introduce the guest speakers and lead the discussion. Tony is the Energy Program Director of Grattan Institute and has extensive experience in the energy sector. He worked for Origin Energy for 11 years and was an advisor on the first Garnaut Climate Change Review. Tony is also a Program Director of Clean Energy Programs at the Clinton Foundation. Please join me in welcoming him.

TONY WOOD: Thank you Sarah and good evening. This is our first event of the year with the State Library. The relationship Grattan has with the State Library is now in its third year and we expect this will be a strong year again, as we’ve seen in the past. In addition to the relationship that Grattan has
with the State Library, the Energy Program also has a partnership with the Melbourne Energy Institute called *The Energy Future* series and tonight that is also joined in co-hosting the event this evening. We've done this before here at the State Library and we sometimes have the events on campus at the Melbourne University. So I would hope that many of you who come here as Members of the State Library will look at the other and think we’re here because of the Energy Institute, but Grattan would also be looking at events that Sarah was talking about in relation to the State Library.

This evening we’re going to try and have some conversation and at some point, either as a result of our comments or the questions that you may ask from the audience, we may get into the area of what’s likely or not likely to happen this year with policy in relation to climate change. A lot has happened in the last 12 months. Many people would say not much has happened at all and, in fact, we were just discussing before we started this evening some of the not quite extraordinary but could easily become so events happening in the United States which clearly could have major implications for climate change policy around the world, despite the events that took place in Paris in early December of last year. So this evening what we really want to do is discuss now that we’ve had Paris and things have settled down, many people would think we’re heading for an election sometime this year and almost certainly that’s true, what does this look like?

To open that discussion we’re going to have short presentations. I’m going to try and set the agenda a little bit and Shayleen and Clare will also do a little of the same, but from their perspectives. I’ve known both the ladies for quite some period of time and they are amongst the most well-informed and experienced people in this sector, both overlapping energy and climate change, that you’ll find in the country. So we’re very fortunate they’re both in their jobs today and they’re both here tonight, because both of them are relatively recently into the roles they’ve taken on, Shayleen as Chief Executive of the Climate Change Authority and Clare in her role as Executive responsible for Energy & Climate Change at the Business Council of Australia which, as many of you would know, is the peak body of the largest companies in this country. Clearly, as many of you will have seen, those companies and their industry associations inevitably have an influence on public policy on a whole range of matters.

So what I was going to do was really just try to remind us all of what the nature of the challenge is. When we call this the hard task of delivering on our international commitment it doesn’t necessarily take a view of whether the commitment itself is hard or easy, although the task of delivering it is, it’s how hard is that likely to be? As Sarah mentioned, I got involved in this stuff seriously in 2008 with Ross Garnaut in the Garnaut Climate Change Review. That seems like an awful long time ago now, yet many of the principles and issues being discussed this year are still the same as were being discussed in 2008. Some things have moved on and some are the same, and one of the challenges I think is which of those are the same and which are different?

So now what do we do having had Paris? I’m going to use more or less the same chart but build it up just to get in front of our minds the numbers, because it’s often the numbers that drive policy and that are driven by policy in relation to this issue of climate change. So this chart basically tracks Australia’s total greenhouse emissions and you can see it’s a bit of a wobbly line, emissions went up and they came down again. And the forecast of the Federal Department of Environment that was published in March of last year, almost a year ago which in the case of a lot of this stuff, as you’ll see shortly, is almost ancient history in terms of how much has changed since, suggested then that our emissions were going to head up pretty significantly between now and 2030. And yet we had already committed to this 2020 unconditional target, this is the target that Australia would meet regardless of what the
rest of the world would do on climate change by 2020, to reduce our greenhouse gas emissions by 5% below 2000 levels by 2020.

So that was the way the world was starting to shape up and then not that long ago one of the key tasks of the Climate Change Authority, which was established to give advice to government on how it should do things like, for example, setting policy and setting targets, was to look at this whole question of what should our targets be? In that context they drew upon the global commitment to keep global average temperature increases to 2°C Celsius and of course, as you know, after Paris the aspiration is now to see what we can do to drive that closer to an increase of no more than 1.5°C. But in the 2°C world the task then was to work out what would Australia’s fair share of that be, and I'm sure Shayleen can comment upon the details of how they arrived at these sort of conclusions, but the conclusion is shown in that dotted red line, and that is that Australia’s emissions reduction should be 45% at least below 2000 levels by 2030.

So you're starting to see a pretty significant challenge if that's what we’re intended to achieve. So that was where things got to as a result of the Climate Change Authority's work and many people will have their opinions on whether that was a big ask or not. This I think is one of the most substantial specific issues to come out of the Paris Conference, and that is that all countries had to make a commitment as to what they would be prepared to achieve post-2020. So the Australian Government set its target and it was, I would suggest, more ambitious than many people expected, but not as ambitious as many people wanted. Certainly not as ambitious in the sense of reducing emissions as the Climate Change Authority's recommended target, but the target is not insignificant, you can see the red line basically is a straight line from where we were through to 2020 through to 2030 and it represents a reduction of 26%, but below 2005 levels by 2030.

So now the numbers are getting a bit wobbly because you're trying to work out what am I talking about here in terms of these numbers, why does it matter what baseline we use? It matters for Australia quite a bit because 2005 was pretty much the mother of all years in terms of emissions in Australia. So if you compare yourself against 2005 then the target looks much more aggressive than it would be if you were comparing it with 2000, which was much lower, or alternatively obviously if you’re talking about along here. So the maths matter if you’re trying to convey a particular view about how serious or not Australia is in reducing emissions. The reality is that compared with most countries Australia is not at the back of the pack. We’re not at the front of the pack, but we’re not exactly leading and we’re somewhere probably towards the back of the pack of countries that have made serious commitments. But it’s a target, it’s not a trivial target, and many people would say it will require significant change.

So to some extent you might argue that it may not even matter all that much in 2016 whether the target is 26% or 45%. It’s a target which is significantly more than where we were, so it’s sort of in this area. So the question then became how are we going? Well, just before Christmas, after the Paris Conference, the Department of Environment released its latest projections of where Australia’s emissions are going and this is this green line here. Now the numbers don't go beyond 2020, but they were certainly suggesting that, given where we are, we're tracking to actually be about 5% to 6% above 2000 levels by 2020, which many people would say, “Well wait a second, doesn't that mean we're going to go above our target?” I won't bore you with the detail, but the accounting of international climate change policy and accounting suggests that no, because of the way the numbers
are calculated it isn’t actually all about how much you hit on a particular day in a particular year, it’s how much you’ve achieved over a period of time.

Australia overachieved in one of its previous rounds of 2008 targets, we can carry forward some of those credits and there are a few other things that they’ve included. The result is that even with that the actual result is pretty close to meeting our accounting target, even though we’ll be above 2000 levels. Now the reason this is important is because it then says to achieve the government’s target, if that’s the target we have to achieve, that’s where we were, then what do we have to achieve to get there? How much emission do we have to take out between 2020 and 2030, even if we’re on track to achieve the 2020 target? The answer is the government thinks it’s about 900 million tons in total in that 10 year period and then you get to the issue of how do you do that? So this 900 million tons on those numbers would be the challenge. Of course, the problem is this is where things were supposed to be going, and so the question is do you believe that we’re actually on this track or do you believe we’re up here? Because that wedge is about 2 billion tons, so for this number to be even anywhere near credible you’ve got believe that we’re already tracking along here.

Now the reason this is important is because when the government announced its policies to achieve its 2030 target it used this chart, which basically shows we have to achieve 900 million tons and this is how we’ll do it. The current government has a suite of policy mechanisms which on these numbers adds up to achieving the 900 million target. So there are two questions to me. One is to what extent is that wedge itself going to turn out to be credible or are our emissions actually going to be higher than? Last year’s emissions in Australia did go up, not down. The second one is do you think these policies, which is the issue we’re going to be talking about tonight, not questioning these policies but exploring the sort of policies that would be necessary to make the sort of changes we’re talking about, to achieve that would be significant?

So this is the list of policies that make up the current government’s direct action, but when you look at this in context, what we looked at and we put out a working paper on this in December, this is what we think are the key issues. There are the criteria that we think in which policies should be judged, they include not just cost but also things like political viability, that is how do you get there from here and is it politically feasible or is it just too hard politically? Secondly, what are the other things you have to talk about? How do you ensure that we don’t adversely affect in inappropriate ways our energy-intensive industries that are also exposed to international competition with countries that don’t have restraints on climate change? This is one issue that we’re certainly interested in discussing tonight, what are the various policies that you could use, including what was Labor’s policy of cap and trade, including what might be the current government’s policy once they move beyond the current mix? Finally, what are the politics really like at the moment, because historically this has been a very toxic debate politically and it’s been the cause of the end of several political careers, including almost the current prime Minister?

So this has been a toxic political debate. The Coalition has opted for a non-trading combination of policies. Labor, as some of you may know, some of you may have already been to Mark Butler’s consultation sessions, is talking about emissions trading maybe not the same as what they had before. You’ve got the Paris Agreement which is still delicately poised as a result of what’s happening or may not happen in the United States and, finally, you’ve got the fact that a number of state governments, including the Victorian Government, are currently looking at what they might do on climate change. Only this week there was a review of the Victorian Government’s Climate Change Act
which talked about a recommendation that the government hasn’t necessarily adopted and may or may not, and that is that the government in Victoria should be setting a target for Victoria’s greenhouse gas emissions. Therefore, what policy would they have and how does a state policy interact with a federal policy?

So this is getting to be the politics of climate change in 2016 and I think the politics are just as important, sometimes even more so, as the integrity of the policies. So that’s where I’m going to leave it, to just give you an idea of what the numbers and issues might be and then ask Shayleen and Clare now to share with you their views from their different perspectives of what this is looking like. Then what we’ll do is we’ll have a bit of a conversation amongst the three of us just to explore that a little bit and give you time to think about the things you’re concerned about, and then, as Grattan always does in these sorts of sessions, we’ll open it up to the audience for a conversation. So thank you very much and I’ll pass over to Shayleen Thompson, who's the Chief Executive of the Climate Change Authority.

SHAYLEEN THOMPSON: Thank you Tony for those very kind words of welcome and, as always, it’s a great pleasure to be here for the Grattan discussion. I’m going to do a couple of things in my presentation. Firstly, we’re slightly here under false pretences, or rather I am. Part of what I’m seeking to do is use this discussion as part of the consultation that the Climate Change Authority is doing on a report we put out in November and we see this event as quite important in that regard. So I’m also going to take the opportunity to say a little bit about the special review we’re currently engaged in and also, on the way through, address some of the points that Tony’s made.

I might start off firstly by talking about the special review, just a bit of a recap for those who perhaps aren’t aware. The Minister for the Environment asked the Authority to undertake the special review, and I guess if you wanted to sum up what we’re trying to do it’s really to have a look at the Paris Agreement and the outcomes that that sets in place, and to look at the set of policies that Australia should adopt to meet the requirements of that Agreement. The review itself though had three elements to it. The first was a report, as Tony alluded to, which looked at the targets that Australia should adopt to meet the requirements of that Agreement. The review itself though had three elements to it. The first was a report, as Tony alluded to, which looked at the targets that Australia should take to the Paris Conference, and that report came out in April last year. The second component was a draft report looking at particularly the emissions trading schemes and exploring those, and that in fact took the form of a policy options paper that came out in November last year and I’ll talk a little bit more about some of the findings in that report. Then the final report, which is due in June this year, is the one that will hopefully wrap all of those elements up together and present the government with a suite of recommendations.

I guess the first point that I’d like to make, and picking up on some of the points that Tony was making, is that you probably have to be living under something of a rock not to have noticed that the climate change policy debate in Australia in recent years has been highly charged and quite contentious. Really what the Authority decided it wanted to do, particularly with the second report or options paper, was just push the reset button on that discussion and see if it might be possible to have a fresh conversation on all of these issues. In that regard one of the things the Authority decided to do was to meet the terms of reference for the special review by really looking at emissions trading schemes, and it's important probably to note that there are many variations on a theme in the context of other policies that could be used to achieve significant reductions in emissions. So what we were trying to do with the options paper that I mentioned earlier was really have the basis or the beginning of a comparative analysis that sought to look at the emissions trading schemes and their various incarnations in the context of other policies that could be used to do a similar sort of job.
So turning now to Paris, and I’m unable to resist making the joke that hopefully we will always have Paris. The Agreement was, of course, struck at the end of the UN negotiations in December last year and is probably the most significant in a range of steps to reduce the risks of climate change. It’s quite a wide-ranging and, I think fair to say, ground-breaking agreement. I guess one of the things that is of particular note is that it has almost universal participation, with almost 190 countries pledging either targets or policy commitments to reduce their emissions. It also has or perhaps strengthens and reconfirms a strong collective goal to limit global warming to well below 2°C and to keep in prospect or to make effort to try and limit emissions 1.5°C. In addition, the text of the Agreement also contains a clear statement of what this will require in terms of when global emissions will need to peak and reduce and achieving net zero emissions by the second half of the century.

So how is all of this going to be done within the architecture of this agreement? The first really key element is a global stocktake every five years to review the cumulative effect of the country targets and, in addition, all countries are asked to review their own target commitments every five years with a view to essentially ramping up the level of admission that each target holds. So it contains the notion that each time you have a review you have to do better than what you said you’d do last time. So the architecture of those successive reviews is actually very important and I’ll come back to them a little bit later on. So turning to Australia’s contribution, the government has set a target, as Tony says, of 26% to 28% below 2000 levels by 2020 and it’s said that it will be looking at a range of policies to meet that target. So existing policies but also looking at some new ones and, of course, some of that work’s commenced already with things like the Energy Productivity Plan which people are working on in Canberra at the moment.

So what does all this mean in terms of options that the Authority’s exploring? I think the take-home message is that we really do need a climate policy toolbox. The terms of reference asked the Authority to have a look at what’s been going in other countries and what other key countries have done in terms of reducing their emissions and, in particular, looking at emission trading schemes and other similar policies. What that’s shown is actually quite interesting I think, as far as I’m aware no country has tried to do the whole of their climate change abatement task with a single carbon price, even those that have taxes and emission trading schemes and so forth. Everyone’s pretty much accepted that you probably can’t cover your entire economy with a carbon price and also that you’re almost certainly going to need other measures to help support and do different things that the carbon price isn’t able to do. So come what may, just about everyone is say, “Oh actually, you’re going to need a raft of different tools in your box to achieve different sorts of objectives”. In particular, one of the things the Authority is doing is looking at what tools are best suited to which task and, in particular, looking at things like different sectors, different gases and different abatement opportunities.

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So I think it’s possible to conceptualise or think about policies in three broad categories. The first one is the market policies, so we have the mandatory carbon pricing policies which make emitters pay directly for their emissions, taxes and emission trading schemes; you have the voluntary options which provide financial incentives to reduce emissions without creating obligations for all emitting firms; other mandatory price-based policies, particular examples of those are things like the Renewable Energy Target and some of the energy efficiency trading schemes, like the white goods schemes that I gather you still have here in Victoria. Moving beyond the market-based policies though, you also have policies that rely on regulation to achieve the mitigation task or information programs to help ensure that consumers have access to the information that they need to make good purchases when they’re buying kit or appliances that consume energy. Finally, you have your
innovation policies, which I think really are geared around finding the new and emerging technologies that will help us reduce emissions in the slightly longer term.

The other thing the options paper did was put together a framework for evaluating the various policies, and these in fact were based on some of the principles in the legislation that established the Climate Change Authority. I’m not going to talk too much about those, they’re not really rocket science, but I think when you’re looking at policies you have to think about whether or not they’re going to achieve the environmental goal you’ve set for yourself. The second is whether they’re able to do it in a cost effective fashion and, finally, there are considerations about equity, so in particular who bears the costs of the policies that you’re looking at? The terms of reference require us to look at international competitiveness - I’m not going to talk about that today because that’s at least ten minutes in its own right - and then, as I said, there’s this issue of best fit and how policies interact.

So I think that if you had a slogan or a buzzword about what we really need to try and do on climate change policy in Australia at this point in time it’s this notion of policies that are both stable and, very importantly, that they’re scalable, and, in a way, that’s exactly what Paris is requiring us to do. The combination of the global stocktake and the five year review that each country needs to go through means that you really do have each five years to look at a progression of what you’ve already put in place. So that means that policies have to be able to be scaled up to deliver an increasing level of emission reductions over time and cost effectiveness therefore is not just about minimising your costs in the near term, it’s also about achieving a least cost transition over the longer term. So the options paper did a little bit of, as I say, evaluation and some comparative analysis and it found that the emission trading schemes, the RET and the energy efficiency trading schemes can be scaled up by increasing targets and caps, or adjusting baselines in the case of emissions intensity schemes. Taxes, obviously you can increase the rate of the tax, and the offsets with government purchase can be scaled up by increasing the budget that’s available to purchase emissions. There then is an issue about what is the cost on the budget that people are willing to bear over time, which obviously needs some consideration.

The options paper I think also noted that electricity may be well-suited to a mandatory price. It’s a homogenous product, a relatively small number of players compared to other sectors, and it’s pretty easy to estimate what emissions you’ve actually got going on in that sector. And of course electricity is very important, it’s a huge share of national emissions, around about 30%, and it offers some really important prospects for mitigation over time, particularly if you think that transport and manufacturing are likely to move more towards electricity than their current fuel sources. But then you get to the question of with respect to a mandatory price, assuming you start off with energy or electricity, how far do you move that coverage out across other sectors? So things like direct combustion, manufacturing, fugitives, which is actually LNG production and, as most of you will know, coal mines. If you don’t do that do you run the risk of distortions? If you do do that, do you have problems in terms of pushing the approach more broadly across those sectors?

Then turning to innovation and information provision, they’re I think very important as well. Probably it’s difficult to give innovation support to achieve short to medium term targets, but it is something that’s very important arguably in the medium to long term. Similarly, information provision, as I mentioned, can be a very important complement to other policies. Just thinking a bit about regulation, over the years I’ve heard various people say, “Oh gosh, why do we have to persist with these market mechanisms? Why don’t we just regulate and everyone will know where they are?” Certainly I think
it’s the case that regulation is a very good approach for some things. So the range of energy efficiency measures cost/benefit analysis and other things have shown how effective they are. The problem is when you try and push regulation across a range of different sectors it becomes difficult to ensure that you’re achieving at least a cost approach that way, which might be seen as a limitation in terms of how far you can scale up.

Finally, just to echo Tony’s points about political stability which goes to the stable and scalable policies, some might argue that there’s a case for considering the set of policies that we’ve already got, recognising that we are where we are now and thinking about how best to effect the transition from here. That's very much a live question and one that we’re very interested in hearing from people about as part of that consultation process for the review. That’s probably all I have time for. If there's a take-home message from today for me, I think they key is that there actually aren’t any unicorns out there, there are no silver bullets. The likelihood is that we’re going to need all the tools in the toolbox working together in the most efficient and effective way that they can if we’re going to begin this huge transformation to a low emissions economy in Australia.

CLARE SAVAGE: Thanks Shayleen. I think you’re right that there aren’t any unicorns out there, although I’ve spent the last ten years looking for one. As Tony said, my name's Clare Savage, I’m the Executive Director of the Business Council of Australian (BCA) responsible for energy and climate change policy. I think, like Shayleen, I’m probably here on false pretences tonight as well. The BCA is mid-conversation, is probably the best way to describe it, on what our views are on Australia’s next options around climate change policy. Certainly we have a 2030 target now which helps to bookend that conversation and to give us a focus, and certainly the BCA is of the view that we don’t yet have the full suite of policy options that we will need to meet certainly our long term targets.

So I’ve come here tonight, I guess, more to talk about how we’re setting up the problem and how we’re thinking about options, rather than necessarily going into what our options may be or what we will think when the time comes. The BCA though is a member of the Australian Climate Roundtable and the Roundtable has acknowledged, as was set out in the Paris Agreement, that if we’re to achieve a goal of well below 2°C, and certainly the ambition is 1.5°C in the Paris Agreement, then this is going to require Australia, amongst other countries, to at some point in time reduce our greenhouse gas emissions to net zero. It’s worth reflecting on that, people talk about it a lot, net zero, it’s sort of thrown around. Net zero is a huge goal to have out there. That effectively means that any carbon emissions or any greenhouse gas emissions we have anywhere in the world need to be fully offset through some form of carbon sink.

From our perspective, we need to be thinking of having conversations like this and engaging with the public on what the right sets of options are for Australia to achieve that goal. Certainly we’ve got the target at 2030 and that is a credible first step, in our view. We will have the opportunity to review that target in 2020 and again in 2025. I think actually in Shayleen’s most recent report the Climate Change Authority makes reference to the fact that the 2030 target will require substantial and sustained effort, and I think that can’t be underestimated. Technology’s going to be critical in all this, so whether grid scale solar becomes cost parity with new coal plants in 2025 or 2035 makes a big difference in terms of the cost of this transition, and we need to be quite conscious of looking at our target and looking at how we can meet it and what the best trajectory is from here to mid-century.
We don’t have a great track record of stable climate change policy in Australia, as Shayleen and Tony both alluded to. For the policy boffins in the room, and I can see a few of you out there, the National Emissions Trading Taskforce, the Greenhouse Gas Abatement Scheme, the Carbon Pollution Reduction Scheme, the Victorian Energy Efficiency Target, the Victoria Renewable Energy Target, the Federal Renewable Energy Target, Clean Energy Future, Emissions Reduction fund – I’ll stop at some point. The question for us is how do we move beyond this? We can’t keep going through a period of having policy reversal after policy reversal and think that we’re going to achieve an investment in environment which actually delivers real change. Certainly I talked about the unicorn at the start and Shayleen also talked about the unicorn, when I was first an economist in Treasury many years ago I thought that emissions trading was the only way to do anything. It was conventional wisdom, but we tried it and we haven’t actually been able to deliver sustainable change so far. As I said, the policy reversals have impacted investor confidence and we probably need a great nuance around the conversation around what will deliver durable and sustainable policy, and I think the Climate Change Authority’s done a great job in its paper of setting out what some of those options look like.

We’ve also got to be conscious of the fact that all of these different policies have had unintended consequences. So we’ve got lots of different sectors in the Australian economy and when we put policies in one that affects another without thinking about it in a coherent way we aren’t helping ourselves to make a smooth transition. So in the electricity market, for example, we’ve got challenges with an oversupply of electricity generation which somehow seems to be coupled with a challenge of investability, because we do still need new investment particularly in renewable energy technologies. That’s having pricing packs and, if anyone really loves electricity markets, South Australia’s a great case study in what’s going wrong here as you’re seeing the exit of thermal generation and the emergency of renewables. The forward price of electricity in South Australia is now double that of Victoria. So we do need to think about how we integrate these technologies and policies going forward.

I put this particular picture up because they agreed on the colour of their ties, so I think there’s hope. But from our perspective what we really want, if I think the BCA wants anything, is policy durability and durability is going to require bipartisanship. I think we’ve seen over the last five years that that’s what’s required and bipartisanship’s going to mean compromise, and compromise is a really difficult word in politics, as most people would know, but compromise will also mean efficiency losses. So I don’t think we should be aiming for the perfect scheme right now. What we need to try is to get a scheme that will achieve our targets, but at the lowest possible cost to the economy and to consumers. As Shayleen said, policies need to be scalable and capable of evolving through time, so maybe we don’t have the unicorn on day one, but maybe at least it’s a horse by 2030, that might be closer. We’ve got a policy architecture here right now that we can build upon, so I don’t think we should be starting with a blank sheet of paper again. It would be nice to go back 15 years and do that, but we’re not 15 years ago. We could have had a carbon price in, what, 2009 if there had been compromise at that point in time. What we need to do now is start with the existing architecture, learn the lessons of our collective experience, and think about how we move forward.

The other thing, if I say “durable” I also say “integrated” a lot. The reason I say “integrated” is because we need climate change policies that are integrated with energy policies and that are integrated with broader economic policies. We need to ensure that they support economic growth and, as Shayleen noted, it’s probably going to be a suite of policies. There’s probably not a unicorn just yet. Carbon
pricing is important, but it's not the only tool. We need to consider whether there are complementary policies which could do some of the heavy lifting in these early years. We want to see a gradual transformation of the sectors that have long asset lives and high abatement potential, and you'll see electricity is a big chunk of that, transport is a big chunk, and built-into electricity is our built environment, so where we live and where we work. Three-quarters of the cars that will be on our roads in 2030 haven't even been bought yet, so as we head towards 2030 and then particularly as we get towards mid-century, we need to be thinking about policies that are capable of supporting the enormous effort these sectors are going to need to do.

So changing the fleet of cars we drive, the buildings we live and work in, the generation fleet that powers our economy, and finding a way where we can significantly reduce our emissions, but at lowest possible cost. We also need to recognise though that the pattern of global decarbonisation is not going to be even and Paris actually reconfirmed that. Each country will have their own targets and they will be differentiated targets and, for many years to come, there won't be absolute targets for some countries. There will be various policies in different countries for how they wish to deliver those targets and to support their local economies. So Australian climate change policies will need to be cognisant of this, will need to think about access to international permits to make sure we keep pace with where international developments are going, will need to manage the impact that our climate change policies have on our energy-intensive trade-exposed industries, and we need to accept that different countries will manage their carbon budgets differently.

So for the BCA in the coming I'm hoping it's a couple of months but it might be much longer than that, we're going to be working with our members, with our key stakeholders, with anyone who's interested, to be honest, to develop a suite of durable integrated energy and climate change policies. What we're looking to achieve is to grow tomorrow's economy while reducing the emissions intensity of our economy and enabling us to meet our future emission's targets, that's 2030 and our longer term target. I've said it and I'll say it again, durable integrated energy and climate change policy, I think I'll say it a lot in the next year, but what we want to achieve, most importantly, is we want an economy that's investable, that's transformative, that's low cost, and that we can regain our energy competitive advantage and that will necessarily be through renewables. Thanks.

TONY WOOD: I'm glad you mentioned the words “durable” and “integrated” because I think we've had policy that's been non-durable and fragmented for quite a while. In some ways it seems to me it is a painful process to give up on the perfect, but then this is fundamentally trying to find how do you get alignment between politics and policy, because this is a politically challenging space in many countries, including Australia. So regardless of what each of us might think is the perfect policy, certainly from a Grattan perspective we've been reasonably consistent and clear that we think the best policy for Australia would be an integrated economy-wide price on carbon implemented probably through a cap and trade, there are variations, but fundamentally a cap and trade emissions trading scheme. But there are many reasons why it didn't happen and we won't necessarily go into all of those, I think many people in the room probably know most of that as much as we do.

So how do you compromise? What do you give up to get an outcome that actually works? If the answer is second-best policy that gets implemented is better than first-best policy that never gets implemented, how much do you compromise and how do you do that? Because it seems to me you open up the whole vested interest question of people will want their compromise, cost, impact on emission intensity etc. So I'd be interested as each of you have been thinking about this, Shayleen
from the work you’ve been doing in your reporting and Clare from the positioning of the BCA, what do you compromise on?

CLARE SAVAGE: The simple answer to that is we don’t know yet. We’re still in the middle of that conversation. The sorts of things that we will need to look at, you talk about carbon pricing and you expressed a view on cap and trade emissions trading, I think there are various forms, as Shayleen acknowledged, of carbon pricing and they’re a continuum. So you might start at one end and it might have the word “baseline” quoted in it. I’m not saying that’s where we’re going but that’s one option, and in 20 years’ time it might look like a cap and trade scheme. There are lots of ways in which these things come into being and I think, as we look at the implications, a really important bit of work that needs to be done is thinking about what’s the total stock of burden on different sectors.

I think what we haven’t done well, and that includes the community, in the past is understood how that burden falls on them and how they experience it and making sure that, as we do design and think about compromises, we are understanding what the implications are of moving away from one solution to ten solutions and taking stock of the cost.

SHAYLEEN THOMPSON: I’d probably answer by using two sectors as a little bit of a case study. So just to revisit a comment in my presentation that, as far as I know, no-one’s tried to push a carbon price across the whole economy, agriculture is a really interesting one in that regard and I’m pretty sure no-one’s tried to do it or has done it with agriculture. There’s probably some reasons for that, a really high number of small entities, family farms, whatever, some challenges, although I think they’re sometimes a bit overstated about that measurement, and also some quite tricky decisions about where you’d put the point of liability if you wanted to have a carbon price over agriculture. So maybe this is an area where you say okay, for the time being at least you’d still have offsets operating in that space, but you might also look to have some innovation support in the hope that finally the silver bullet of the methane vaccine, after 15 years of being in prospect, gets into operation.

The other case study I’d point to is energy efficiency. Most people would acknowledge that until a carbon price gets up really, really high you’re not really going to be able to address some of the nice non-price barriers that you find in terms of energy consumption. You’ll probably know them quite well, there’s the information asymmetry problem, the split incentive landlord and tenant-type problem, and also the fact that in some companies and firms still getting energy efficiency savings up to the attention of the Chief Executive and the board’s quite challenging. So all of those things draw you, I think, to the conclusion that actually you need other policies to try and capture some of those benefits and some of those savings, because there are a raft of studies that show you that you can achieve a lot of energy efficiency at what economists somewhat confusingly call negative costs.

So I suppose my response, Tony, is that maybe you don’t need to necessarily compromise. Maybe part of what you need to do is really look at best fit per sector and, at the risk of sounding a bit like a stuck record, put in place this toolbox kind of approach.

TONY WOOD: And maybe that’s the practical way forward, given that we don’t seem to be in a position that’s going to end up with the perfect policy. Certainly history would suggest that and when you look at the various policies that people are implementing in other parts of the world they tend to have that mix, and presumably for their own local political issues as well just as much as the sort of issues that would result to is there a better way?
One of the things that I certainly think and many others have commented on, I mentioned before about when you start compromising it opens up the door for vested interests and rent-seekers and whatever you might want to call the organisations who would put that, but I think one group that would be accused of that would be industry. One of the things that set off the original emissions trading approach back in what was the golden era of climate change policy in Australia, an era which lasted probably about two-and-a-half years, was that at the time, in addition to the difficulties that the government had with the changes of leadership, the opposition and so on, and the Greens, there was also the issue of business who was pushing back very heavily on the approach that the government was taking. And I wouldn’t want to verbal the BCA, but I think the BCA at the time was supportive of some of the principles of emissions trading.

So do you think that world has changed? There were a lot of businesses at the Paris Conference and a number of businesses have been starting to publically call for carbon pricing around the world. So a) would you argue that business has changed, since you’re now part of an industry association, and b) is that likely to help the process of actually moving forward on policy that isn’t so toxic or partisan?

CLARE SAVAGE: I think if I had a dollar for every time I’d been called a rent-seeker I’d be a wealthy woman. I think everybody’s moving on in this debate, would be my observation. I think some of the core issues will remain. A core issue for all Australians should be whether or not our emissions-intensive trade-exposed sectors are having comparable treatment to our trading partners, and that’s a matter of jobs for all Australians. So I think that will remain a big issue for industry, but certainly I think when I said “compromise” I think everybody’s in the compromise boat. If you’d looked at the BCA’s position, and I wasn’t there then, back in 2009/10/11 it was about well-designed cap and trade emissions trading. We’re certainly having a much broader conversation than that now.

TONY WOOD: Okay. Those couple of questions were based on some of the things I’ve observed and your comments, and we did have several questions submitted online directly before tonight’s event. I’ve got quite a few more that I can use if I need to, but now might be a good time to throw it open to you to ask some questions around the issue. Would anybody like to start off?

AUDIENCE: My question is to Shayleen, none of your policy measures involve building renewable generating plants. We built the Snowy Hydro Scheme however many years ago. I don’t know what level of government it would come under, state or federal, but there’s nothing about actually building renewable energy-generating plants.

SHAYLEEN THOMPSON: So just to say a little bit about who we are. So the Climate Change Authority is a statutory authority that was set up by legislation in 2012. Our role is to advise government and the parliament on climate change policy and it generally turns around particular reviews, including often of legislated schemes like the Renewable Energy Target. So I think your question is about policies that would create a direct financial incentive for building renewable energy plants, and I guess there are a number of different ways that you can do that. One of the obvious ones that we have at the moment is the Renewable Energy Target, that of course has had a somewhat chequered history, but there’s nothing about actually building renewable energy-generating plants.

Climate policy in 2016: The hard task of delivering on our international commitment
Melbourne 16 February 2016 – Edited transcript, transcribed by Bridie’s Typing Services  p.12
that gives targeted loans to people that are wanting to invest in a whole range of activities including renewables. There’s also ARENA, which is the body that provides grant funding to renewables. So I think one of the things the Authority is very interested in looking at and hearing from you on is what else more different would you need? I guess the other point that one probably should make is that a carbon price will also create a financial incentive for renewable energy because it creates a definite incentive for cleaner low emission energy compared to other forms.

So I’m very interested in hearing what you think the optimal policy suite would be to incentivise more investment in renewables.

AUDIENCE: I’ve a question for the panel about what your views are about the integration across federal, state and local levels and, in particular, across different industries. For example, given that climate change involves not just energy but involves water and building codes, these are under the jurisdiction of different levels of government. How do you plan on integrating and co-ordinating a systems approach to climate change?

TONY WOOD: I think the first thing you do is not start from here in a sense, because in the same way that we haven’t had integrated energy and climate policy, we’ve certainly not had integrated state and federal policy in this area. My concern in 2016 is that could get worse. This is by no means a forecast, but I think that the federal government has made it clear that as far as they’re concerned they have a policy and they will review that in 2017 if they are in government, and the Labor Party is consulting on a policy including on a target. So in the absence of that, as we saw once before, and Clare referred to this, some years ago the states became quite agitated and started to do their own thing on climate policy. And that could be quite nasty because you end up, with good intent, creating policies that actually clash together quite badly and produce some really unexpected outcomes, most of which are not good either environmentally or economically.

That’s not to say that there are not roles for state governments or local governments because, as you said, there are certain levers that certain governments can pull in our federal system and in our local government. But I think it’s critically important that they are seen in the right context, so it wouldn’t make sense, I wouldn’t think, for state governments to be doing things that are not consistent with federal policy. They should be looking to influence federal policy through the mechanisms they have politically despite that frustration and, equally, at local government level. For example, the Melbourne City Council and other councils around Melbourne do have quite a few programs, but they should be thinking about it, I would suggest, in the context of the way business thinks about it.

What are the things that we’re doing that we would do differently if the world was seriously adopted a climate change target? What are the things we would do differently? The decision we’re about to make on the way we’ve zoned Fisherman’s Bend in Melbourne, would we do something differently if the world seriously and Australia seriously was going to do what’s necessary to have the sort of impact that $100 a ton carbon price would have? You might conclude that the things you would do would be different and that’s where I think that conscious thinking about policy is important. My worry is that I don’t know that’s the way they’ll go about doing it because I think the frustration levels might be too high.

SHAYLEEN THOMPSON: We were talking a little about Groundhog Day on climate change policy in Australia and I was reminded that some years ago a former colleague of mine launched a major
review of all the policies that the states had in place to address climate change at that time. Because
an emissions trading scheme was about to be implemented everyone duly went through a process,
did cost/benefit analysis, looked at whether their policies stacked up and whether they should keep
them, and in fact a number of states got rid of some of those and actually, as Tony’s saying, people
are now busily thinking about and in some cases actually reintroducing them.

So I agree, it can be really very problematic and it tends not to be terribly efficient. That said, I think in
our first report on the targets we noted that nature abhors a vacuum and people will step in to take
action if there’s a perception that there aren’t things happening. I think it’s a difficult one. Some of it I
suspect is actually part of the joy of being in a federation, and I’m not sure that there’s an awful lot
that we can do about that really.

AUDIENCE: I’m just wondering what lessons we can take from other countries that have had
successful climate change policies implemented. Germany always comes to mind straight away and it
seems to be a country that Australia wants to emulate in terms of moving the economy away from
being solely reliant on resources and things like that into innovation. I’m just wondering what lesso
ns we can take from them and why they’ve been successful while we haven’t?

CLARE SAVAGE: Germany’s an interesting case study and I think it’s questionable how much
success they’ve had. Certainly as they have wound back nuclear and started to import coal from the
US their emissions are turning around. They have been part of obviously the European movement
and they’ve also had similar issues with integrating renewables. So I think from my perspective one of
the challenges is I look around the world and I struggle to see really good examples of climate change
policy because I think we’re all on the same journey. Probably Australia’s has been a little bit more
amusing from an external perspective, but we’re all grappling with the same kind of challenges from
what I can see. But you might have a different view?

TONY WOOD: I would certainly reiterate what Clare said about you might define success very
carefully I think. The other thing to remember is that the physical context makes an enormous
difference around climate change. So in the case of Germany, they sit in the middle of the European
system with lots of interconnections. In theory the EU has a common view about climate, but then
when you look at what’s actually going on you’ve got some countries that have got a very high
penetration of both onshore and offshore wind, for example, while others have got nuclear and so on.
So when they then try and balance that system that whole system works reasonably well together,
although you may be aware there’s a lot of financial stress going on in the European energy system,
including particularly in Germany. There have been big questions as to how they’re going to survive
that process, but they may.

So there are certainly things you can look at that you wouldn’t do in many countries in the world.
Unfortunately we’ve tended to import a few of the things that probably weren’t such a good idea from
other countries and we’re now trying to backtrack from those, but the nature of the Australian system
in that we’ve got 24 million people today in a very small part of the country, scattered around the
edge, mostly in a small number of cities with a lot of distance between them, and some particular
areas of resources that we use for energy have a lot of influence on the way we think about our
policies and how we get from where we are now to where we need to be. So specifically an example
is the challenge that we’ve already seen a little bit of in South Australia where you’ve got a state with
a very high penetration of wind and solar, yet dependent increasingly on the connection between South Australia and Victoria, and how that connection works or might not work in the future.

So it’s not as though you don’t do it, but you’ve got to go into that with your eyes open, and that’s not a situation that you see in other countries. So we’ve got that challenge and I think that’s why we need to learn carefully, because taking something that someone else has done and assuming it would work in our context, in both our federal system and our physical system, is risky.

AUDIENCE: An observation about the tone of the discussion, one of the things that has, in fact, changed is we now have a much more ambitious global agreement. It’s kind of known that that agreement itself is going to ratchet up and even Australia’s commitment to it is in pursuit of an agreement that’s going to way overshoot the 2°C target. So the only way it’s going to go is to become more ambitious over time. A lot of these discussions are about the need for a blend of policies which obviously needs to happen, but it’s almost like a defeatism about the carbon tax didn’t work or the baseline credit emissions trading scheme would be ideal. I just wonder if the urgency of the issue has now got to the point in terms of the public narrative where those things can actually be back on the table a lot more than all of us who’ve been working in this field for a long time have come to accept as the normal? Maybe the issue has been framed too much in the pre-Paris mindset, but the world has actually moved on and we need to catch up with it.

TONY WOOD: Yes. Shayleen, has the Paris Agreement influenced the way you’re thinking about it?

SHAYLEEN THOMPSON: Yes and no, in the best Sir Humphrey fashion. I think Paris, you’re exactly right, you said it puts in place this architecture that really calls for increasing ambition given that the pledges on the table at the moment aren’t enough to get you to 2°C. Paris itself though is silent on the mechanism as to how you get there, and that’s going to remain a question for all of the countries as they go forward. Indeed, some of the more pessimistic commentators are saying that actually the reason why there’s a range of, I think, 2.7°C to 3.6°C about what the pledges mean is actually because it’s not clear how some countries are going to get to meet their targets. In terms of things being on the table, you probably have to draw a distinction between judgements about what may or may not be politically feasible in the short to medium term and what may or may not be seen as best policy.

So I think what the Authority is genuinely trying to do is to look at the policies on the table and in the toolbox and then advise the government on which of those will be best. I guess one of the points I was trying to make earlier on was that if you look at the mandatory pricing options in particular, in some ways they actually have more in common than they have that’s different. They’re all trying to create incentives for action, encourage fuel switching, encourage people to take action to reduce their emissions and to find those emissions at lower cost. Then you start getting into some very fine levels of gradation around which of those is best. The Authority hasn’t formed a view on this, but I think if you read some of the commentators, and in particular some of the work that Grattan’s done, the point there is the choice you make about which of those approaches you might prefer is partly informed by what you might see as a political economy set of considerations.

So what I’m trying to say is I think, for the Authority anyway, all the options are on the table are being very explicitly considered. The only point I would make is that the point about the toolbox is really saying, “Do you really think you can do everything you need to do across the whole of the economy with just a single measure?” Because all the experience is suggesting that actually you probably are
going to have uncovered sectors and you also might want some, what people used to call, complementary measures to try and bolster what your carbon price is trying to do. Then there is I think a genuine discussion about do you want to keep relying on a more voluntary approach, like the emission reductions fund and the safeguard mechanism, or do you need to think about transitioning to something that looks a bit different to that?

CLARE SAVAGE: Just to add to that, if I’ve given you a sense of pessimism I apologise. I feel really optimistic about the fact that the Paris Agreement was achieved and that’s why I think bipartisanship’s in sight, but I think the path to that means we just keep moving forward. So from our view, rather than starting all over again, because we’ve done that now so many times, let’s take what’s in front of us and push on. So I think that’s more what I’m saying, rather than we’re all ruined. It’s not that; it’s let’s build that momentum and keep moving.

TONY WOOD: It feels to me like many people in government and the organisations that we work in, and many of you may also have views on this, is that many of us have been arguing we need to climb a mountain and we’ve been going around working out how we’re going to do it. There’s a whole lot of people who don’t even believe there’s a mountain there at all and the reality of Paris is that not only is there a mountain, actually it’s been getting higher while we’ve been talking about how we start to climb is, so wouldn’t it be a good idea in 2016 to actually start climbing? Now whether the mountain is as big as some people think or a bit smaller, it almost doesn’t matter all that much provided we start climbing the right mountain and are more or less getting to the top.

So I think the thing that gives us a bit of optimism is that, firstly, countries like Australia, where it’s been politically divisive, actually did set a target, and we have a post-2020 target which was a significant move. Secondly, you’ve got, with all its warts and all its problems and all the things that might still unravel, the Agreement itself, so there’s a sense of optimism there. No-one claims, including the government, that the Australian target is enough to achieve the 2°C let alone the 1.5°C, but at least we might make a start. Therefore what becomes critically important is that we have the beginnings of bipartisan support in how we’re going to do it. It doesn’t have to be whether or not we want a perfect emissions cap and trade scheme, but broadly speaking we’re going to employ, even if they aren’t perfect, several things that are going to head us in that direction. That’s where the reality of this year is I think really.

ROSS GARNAUT: A couple of points, I think the discussion’s been too pessimistic. We had a very important discussion about the difficulties of integrating state and national policies. When we had a national carbon price covering most sectors and supported by uncontroversially implemented policies in relation to innovation support through ARENA and financing support through the CFC, we had a quite rapid dismantling of the state policies. All of the state feed-in tariffs disappeared and the state governments focusing on the things where the states had comparable advantages, especially adaption. When we got rid of the national policies, carbon emissions started rising again from July 2014 and then naturally the withdrawal of effective national policies meant that we returned to the dog’s breakfast we had before. But the fact that we were getting a nationally integrated policy around national carbon pricing shows that it’s not impossible. The main point I wanted to make was I want to
take up Shayleen’s invitation to participate in her public discussion. I’d just like to make one point there, but before I do that, congratulations Shayleen and to the Authority for battling on in the most difficult circumstances over the past couple of years. Now that the sun’s shining a little bit I hope that life can be easier. It’s been tremendously important that the Climate Authority didn’t give up in those dark days.

The point I’d like to make is there’s been a little bit of sympathy or a little bit of feeling on the panel that carbon pricing was hard because it created an opportunity for organising a political campaign around its support, so something else will be better and something else is sometimes described as a baseline and credit scheme perhaps around average intensities. But if you design a dog and then you build it then it’s going to bark like a dog. Your hope that it might be a cheetah or a different sort of animal are not going to be realised if you’ve designed it like a dog. There are a number of problems with using the baseline credit scheme as a basis for widespread emissions. The first is it’s very hard to generalise beyond the more homogenous sectors like electricity where the idea of emissions intensity is easily applied. Elsewhere you’re involved in a highly intrusive process of setting baselines, but even in the electricity sector there is a pretence that conflicts with every lesson of economics, that somehow if you don’t make the liable entities pay for the carbon credits then they won’t pass on to consumer this scarcity value of the emissions permits, of the credits.

Now every bit of economics we’ve ever learned tells us that the extent to which a baseline and credit scheme will be effective will be the extent to which it creates scarcity of emissions entitlements and the amount of emission reductions will be associated with the price of that scarcity. So for the same amount of emissions reduction you’ll get the same increase in price, as with a carbon tax or an emissions trading scheme. Obviously, if you do less in reducing your emissions you’ll have a smaller price effect, but the price will be passed on whether or not you’ve paid for permits. The difference between the schemes is that the budgetary effects of a carbon tax or an emissions trading scheme with option permits are very positive, whereas they are not for the baseline and credit. The other difference is that the income distribution effects are perverse. The carbon tax and the emissions trading scheme create revenue which can be used to compensate either trade-exposed industries or low income households, as they were in the carbon pricing scheme of 2012 to 2014. In the case of baseline credits there’s a straightforward transfer from the household sector to the generators, especially the low emissions intensity generators.

As soon as you start to do that there will be a political problem. There was a political problem even with the carbon pricing scheme that completely compensated the bottom half of the income distribution. There will be a much bigger political problem if there is a real not an imaginary transfer from low income households to the corporate sector. So Australia’s big economic problems at the moment are problems of the budget, the baseline and credit is a difficulty for the budget, the others contribute positively to it. The other is the worsening income distribution that’s given declining real incomes to ordinary Australians since 2011. Both of those central problems of Australia would be made much worse with baseline and credit, but they’re not made worse with a carbon tax or an emissions trading scheme. So that’s my submission Shayleen.

SHAYLEEN THOMPSON: Thank you Professor, that was very comprehensive.

TONY WOOD: My only response to that really would be that Ross is highlighting that when we start this whole process of accepting that we might need to compromise, for whatever reason, it is a
difficult path. All the issues that Ross has raised will come out in spades and working out how you get there and whether you get stuck on the way, because you might go down what appears to be an attractive way to avoid some of the concerns that have emerged with cap and trade in other parts of the world or even in Australia, and then you get stuck and you can’t get back to where you want to go. All these issues are going to be the sort of things that have to be properly talked about before we go down any particular path. Clare, did you want to make any comment to Ross?

CLARE SAVAGE: I took it as a comment, but the issues that Professor Garnaut has raised are well-articulated I think in the Climate Change Authority’s report. Certainly I think there are some of the issues, such as Professor Garnaut’s comment that he made about whether or not permits are treated as a production subsidy, that will also impact whether they’re passed on in prices and there’s a nuance there that we probably need to work through.

TONY WOOD: With that fairly extensive discussion around what is going to be a central part of the debate that takes place, we’ve extended just slightly beyond the intended finish time for this evening. It really only is for me to thank you all for being here this evening and to thank the State Library for hosting us at the venue once again. I would certainly encourage those of you who are on the Grattan or State Library mailing list to look out for the next Policy Pitch at the State Library. Equally, you’ll certainly see both Grattan and the Melbourne Energy Institute undertaking some further activity here or more on the university side of things on our Energy Future Program in 2016. Finally, could you please join me in thanking Shayleen and Clare for being part of the panel tonight? Thank you.

END OF RECORDING