Submission
No 10

COGENERATION AND TRIGENERATION IN NEW SOUTH WALES

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The Chair
Public Accounts Committee
Parliament House
Macquarie Street
SYDNEY NSW 2000

By email: pac@parliament.nsw.gov.au

Dear Sir/Madam,

AGL Energy Response to the New South Wales Parliament Public Accounts Committee's inquiry into cogeneration and trigeneration

AGL Energy (**AGL**) welcomes the opportunity to provide feedback to the New South Wales Parliament Public Accounts Committee's (**Committee's**) inquiry into cogeneration and trigeneration in New South Wales.

As a leading investor in renewable energy and one of the largest energy retailers in Australia, AGL is well placed to comment on the issues that the Committee will consider as part of its inquiry. AGL operates across the supply chain and has investments in coal-fired, gas-fired, renewable and embedded electricity generation. AGL is Australia's largest private owner, operator and developer of renewable generation in Australia. AGL is also a significant retailer of energy with over 3 million electricity and gas customers.

AGL supports the existence of a regulatory and commercial environment that is conducive to the development of cogeneration and trigeneration projects. AGL considers the development of such projects to be an important service that it is able to offer to its larger industrial and commercial customers. There are a number of barriers that prevent the development and growth of cogeneration and trigeneration. The most significant of these are:

- high gas prices and the prospect of a significant gas shortage in New South Wales, combined with an oversupplied wholesale electricity market, reduce the commercial incentive for parties to consider alternative, gas-dependent, options such as cogeneration and trigeneration;
- pre-registration and connection costs can be disproportionate to the size of the cogeneration/trigeneration project; and
- the lack of available funding under existing State or Commonwealth clean energy or energy savings programs for the development of cogeneration and trigeneration projects, for example:
    - the inconsistency between the Build Own Operate model under which many project developers (such as AGL) build cogeneration and trigeneration facilities, and the funding eligibility criteria under the Commonwealth Clean Technology Investment Program; and
    - the removal of the New South Wales Green Business Program that previously provided funding to cogeneration projects in New South Wales.

New South Wales Government must as a priority address gas supply shortage

Increasing gas prices will be exacerbated by significant gas shortages that threaten to face New South Wales by 2015 unless the New South Wales Government acts immediately to change relevant policy settings to stimulate new sources of gas supply. Combined with an oversupplied electricity market, there currently exists no incentive for the development of cogeneration and trigeneration projects. Furthermore, the carbon pricing mechanism has not yet had a sufficient impact on electricity prices to incentivise cogeneration and trigeneration developments.

As part of a broader reform agenda for the gas industry which will also have the effect of creating market conditions that are more conducive to cogeneration and trigeneration, it is vital that the New South Wales Government takes immediate action to enable increased gas supply to be realised in the State. If no action is taken, gas shortages that are expected to be experienced on the east coast of Australia within the next 12 – 18 months with the development of LNG export facilitates in Queensland, will have their most dramatic impact on New South Wales given that:

- New South Wales imports around 95% of its gas supply from South Australia and Victoria;

- Long term gas supply contracts into New South Wales start expiring in 2015, and drop dramatically by 2017 leading to demand being significantly in excess of supply;

- Existing contracts out of South Australia are unlikely to be rolled over given that the vast majority of this gas is committed to LNG export facilities; and

- Victoria is not a viable substitute source of gas into New South Wales given that existing pipeline and gas processing capacity are insufficient to meet peak demand levels in New South Wales.

A failure by the New South Wales Government to take steps to ensure new sources of gas supply will lead to a real risk that current levels of gas consumption in NSW will not be able to be maintained in the future. This will necessitate (in some cases, permanent) exit from the market in order to bring consumption into line with available supply. It also risks leading to a significantly reduced dispatch of gas-fired electricity generators and a removal of the ability and incentive for the development of cogeneration and trigeneration, and an increased dispatch of existing coal-fired plant in New South Wales.

Accordingly, it is imperative that the New South Wales Government takes steps to:

- remove all ad-hoc, non-scientific, planning and 'green tape' barriers to the exploration and production of gas; and

- set a clear and achievable coal seam gas framework which would facilitate safe and orderly development to continue in order to satisfy New South Wales gas demand.

This would allow more reserves to be developed, which would lead to a reduction in pricing pressures for large customers over the medium to long-term which would also contribute towards the creation of market conditions that are conducive to the development of cogeneration and trigeneration in New South Wales.

Disproportionately large pre-registration costs

The costs of modelling and pre-registration activities that are required to be undertaken by project proponents prior to registering a cogeneration or trigeneration facility with a network can be prohibitive and disproportionately large compared with the cost of the project itself. It would be helpful and would not compromise overall network safety if costs were more effectively scaled so as to require less comprehensive modelling at the network level for smaller generation equipment.

Funding structure of the Clean Technology Investment Program

Funding arrangements under the Commonwealth Clean Technology Investment Program are inconsistent with the Build Own Operate model that AGL (and other parties) operate on the basis of. This model involves service providers (often energy companies) building and owning projects such as cogeneration or trigeneration facilities at customers' sites, and selling the electricity output back to the customer. This is an efficient model which enables the development and maintenance of facilities by parties that are expert at doing so and which generally have access to gas on better terms than entities not involved in the energy industry.

However, in AGL's experience, developers of cogeneration or trigeneration projects under this model are ineligible for funding under the Clean Technology Investment Program, on the grounds that the builder of the project is not the ultimate beneficiary of the electricity produced. This significantly disincentivises the development of efficient cogeneration and trigeneration projects, instead encouraging such projects to be built on terms and adopting methods that are potentially sub-optimal by parties with little experience in undertaking such development.

The expansion of program funding entitlements to third parties adopting a Build Own Operate model would encourage the development of cogeneration and trigeneration projects by parties that are the most expertly skilled and best equipped to efficiently build such projects.

Concluding comments

Current energy market conditions in New South Wales in which there is an oversupplied wholesale electricity market and increasing gas prices disincentivise cogeneration and trigeneration. This is set to become worse with expected east coast gas shortages likely to impact New South Wales most significantly. Such an extreme scarcity of gas in New South Wales will constitute the most significant barrier to such projects occurring.

Therefore, in the interests of New South Wales' broader energy security needs and economic stability, and to enhance or at least maintain the social and economic wellbeing of its residents, it is imperative that the New South Wales Government addresses the gas supply shortage expected to impact the State by 2015 as a matter of priority by undertaking reform initiatives that will expand current sources of gas supply. This will, over the medium to long-term, reduce pricing pressures likely to be faced by large gas users, and create market conditions that may ultimately be more conducive to cogeneration and trigeneration projects.

In the meantime, expanding the New South Wales Energy Savings Scheme to include cogeneration and trigeneration projects would incentivise such developments by rewarding the energy savings that that such projects deliver and encouraging the development of such technologies.

Should you have any questions in relation to this submission, please contact me on [redacted] or [redacted] or Anita George at [redacted] or on [redacted]

Yours sincerely,

[redacted]

Tim Nelson
Head of Economic Policy and Sustainability