INFRASTRUCTURE PARTNERSHIPS AUSTRALIA

8 November 2018

Energy Division
Department of the Environment and Energy
GPO Box 787
Canberra ACT 2601

Via email: UnderwritingNewGeneration@environment.gov.au

RE: Submission on the Underwriting New Generation Investments proposal

Infrastructure Partnerships Australia welcomes the opportunity to make a submission on the Underwriting New Generation Investments consultation paper.

The Department of the Environment and Energy's consultation paper correctly highlights the risks of government intervention into energy markets. This submission further explores these risks and provides evidence around the current investment environment within the energy sector.

Australia's energy sector is experiencing a period of considerable disruption, in terms of technological change and new business models. Within this context of disruption, ongoing policy uncertainty has exacerbated challenges in attracting investment into new generation within the National Electricity Market (NEM).

Recommendations

1. The Federal Government should pause consideration of the Underwriting New Generation Investments program, until after agreement has been reached on a broader national energy policy.
2. The Department of the Environment and Energy should publish a detailed cost benefit analysis of the Underwriting New Generation Investments program. The analysis should examine the costs of over-investment in generation assets and distortion of investment incentives.
3. Should the program proceed, the Federal Government should present a clear and transparent summary of the financial risks borne by taxpayers for each transaction, at the time of execution and for the life of the liability.

Investor uncertainty

The stated objective of the Underwriting New Generation Investments proposal is to enable greater investment into energy generation assets, to enhance competition within the NEM, which will in turn improve affordability and reliability for consumers. Acknowledging this overarching objective, we submit

Suite 3.03 Level 3, 95 Pitt Street, Sydney NSW 2000
PO Box R1771, Royal Exchange NSW 1225
T +61 2 9152 6000 **F** +61 2 9152 6005 **E** contact@infrastructure.org.au **www.infrastructure.org.au**

that direct government intervention in energy markets is likely to distort incentives for investment in energy generation, and may act counter to this stated objective.

We are therefore concerned that the proposal may undermine the National Electricity Objective, which is:

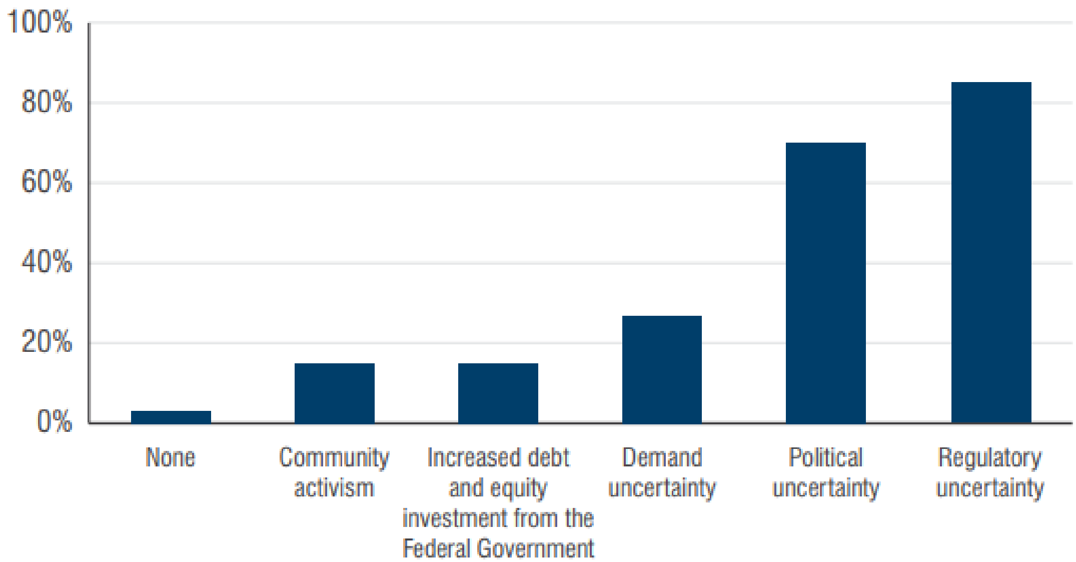
> "to promote efficient investment in, and efficient operation and use of, electricity services for the long-term interests of consumers of electricity with respect to:
>
> - price, quality, safety and reliability and security of supply of electricity
> - the reliability, safety and security of the national electricity system."

We submit that the long-term interests of consumers would be better served by progressing a national energy policy, rather than further direct market interventions.

We recently released the *2018 Australian Infrastructure Investment Report* in partnership with Perpetual. The report provides a comprehensive view of global and domestic investor appetite and sentiment.

This year's investor report contains a section focused on the key challenges and opportunities for investors in the energy sector, and as such provides timely and relevant evidence, as to the real causes of the current softening in investor appetite for energy generation assets. The report explains that political/policy uncertainty and regulatory uncertainty are the two biggest factors limiting investment in the energy sector (see Figure 1).

Figure 1: Factors limiting investor interest in the energy sector



Source: 2018 Australian Infrastructure Investment Report

Our research shows that the ongoing lack of policy certainty and multitude of government interventions has had a dampening effect on investor appetite, with one investor explaining that:

> “Governments are constantly changing the rules and it seems to be driven by very short-term reactionary policies impacting much longer-term investments. One needs to be pretty brave to underwrite investments predicated on a policy which could change.”[1]

With reference to this evidence on investor sentiment, we submit that the risks highlighted in the consultation paper such as distortion of debt markets for generation investment and the possibility that intervention will have a dampening effect on investment are very real. For this reason we recommend that the Federal Government pause consideration of the Underwriting New Generation Investments program, until after agreement has been reached on a broader national energy policy.

Risks to taxpayers

As highlighted in the consultation paper, direct government intervention in energy generation assets risks transferring investment risks from investors to taxpayers, risks which taxpayers are not best placed to manage. Moreover, by underwriting new generation assets, the Federal Government risks incentivising over-investment in generation, the cost of which will also be borne by taxpayers.

The Productivity Commission’s *2015-16 Trade Assistance Review* warned of these risks as part of its assessment of similar proposals for intervention into energy generation markets by both state and Federal governments.

The Productivity Commission provided clear analysis of the risks to taxpayers of governments intervening in energy markets, stating that:

> “Whether these projects will proceed is uncertain, but there is a risk that they will lead to the wrong infrastructure in the wrong place and the electricity consumer will end up paying higher prices as a result. The more that market forces dictate what and where, the less likely that the investments will end up as white elephants.
>
> Government investment in electricity market assets can result in assets that do not have to earn a commercial rate of return. This can undermine competitive neutrality. More problematically, such entities have in the past provided energy at below market prices to some ‘base load’ customers (Turton 2002).
>
> Accordingly, it is important that any proposals be carefully evaluated, and that consideration be given to alternatives that might address emerging problems in the electricity market in a more efficient and less costly manner. A risk, otherwise, is that future generations of taxpayers will be called on to foot the bill for precipitate responses to perceived crises now.”[2]

The Productivity Commission’s analysis makes several important points about the risk of over-investment and the wrong type of investment. However, it is also important to note that the Federal

---

[1] Infrastructure Partnerships Australia and Perpetual, 2018 Australian Infrastructure Investment Report, 24 October 2018, p. 17.
[2] Productivity Commission, *2015-16 Trade Assistance Review*, 2017, pp 57-58.

Government will be entering into contracts on behalf of taxpayers that private investors would reject due to the inherent risk of these investments.

If the Federal Government does move ahead with the proposal to underwrite new generation assets, it is essential that taxpayers are made aware of the risks being taken on their behalf. For this reason, we submit that the Federal Government must provide details of the risks taxpayers are exposed to at the time of each transaction. This quantification and transparent disclosure should be maintained for the life of the liability.

Conclusion

As Australia's peak infrastructure body, representing public and private infrastructure owners and operators, we are pleased to contribute to this consultation process and respectfully request that the impacts of the proposal to underwrite new generation assets be carefully considered within the long-term context of the energy market.

As a final comment, if the proposed measures do proceed, it is essential that the taxation implications of these measures are appropriately considered to ensure no adverse impacts on project economics. The Infrastructure Partnerships Australia Taxation Taskforce would be happy to engage with the Department of the Environment and Energy and Treasury at the appropriate time to discuss the taxation implications on projects.

Thank you for your consideration of this submission, if you require any further detail please contact Robert Montgomery, Head of Economics and Policy, on (02) 9152 6021 or robert.montgomery@infrastructure.org.au.

We would also be pleased to provide a more detailed in-person briefing on the insights contained within the *2018 Australian Infrastructure Investment Report*, if you would find it of use.

Yours sincerely,

Adrian Dwyer

ADRIAN DWYER
Chief Executive Officer