Investor Group on Climate Change (IGCC)

Submission to:

Senate Inquiry on the Grid Reliability Bill 2020

September 2020

Erwin Jackson, Director, Policy
erwin.jackson@igcc.org.au
www.igcc.org.au

ABOUT US

The Investor Group on Climate Change (IGCC) is a collaboration of Australian and New Zealand investors focused on the impact that climate change has on the financial value of investments. The IGCC represents institutional investors with total funds under management of over $2 trillion, and others in the investment community interested in the impact of climate change. IGCC members cover over 7.5 million people in Australia and New Zealand.

Summary

The Investor Group on Climate Change (IGCC) welcomes the opportunity to make a submission to the Senate inquiry into the *Grid Reliability Fund Bill 2020* (GRF Bill).

Institutional investors have systemic exposure to climate change risks. A managed transition to net zero emissions by 2050 and actions to build resilience to the impacts of climate change will reduce the cost of climate change and open up investment opportunities. Long-term investors have a critical role in delivering this more prosperous future and are increasingly changing their investment practices to align with a net zero emissions economy. However, investors can't address climate change alone. Governments have an obligation to implement policies that are credible, durable and predictable. This will reduce financial risks and encourage investment in low and zero carbon opportunities.

IGCC's comments on the proposed GRF Bill are:

1. IGCC supports the overall policy objective of the Grid Reliability Fund.

2. The Government must embed grid reliability considerations and other changes to the Clean Energy Finance Corporation (CEFC) in a strategy to achieve net zero emissions by 2050 to unlock private capital in a broad range of net zero emissions technologies on the scale required.

3. The Government and the parliament should examine the GRF Bill in the context of the other climate change policies as they will have a material impact on the success of the CEFC in unlocking private sector investment (e.g. expanding the mandates of the CEFC and ARENA, climate resilience measures and the development of Australia Long-Term Strategy under the Paris Agreement). For example, legislative changes to the CEFC's mandate should be considered alongside examination of the GRF Bill to ensure a coherent package of measures are implemented. Additionally:

    a. The CEFC's mandate should also be expanded (with additional funding) to include developing financing solutions for climate change adaptation.

4. Regarding the expanded definition of low-emission technology, the CEFC should publish it's criteria for 'a low emissions electricity system' to provide further transparency on decision making. Such criteria should include that the CEFC can satisfy itself that the investment is in line with the objectives of the Paris Agreement.

5. While IGCC supports the changes to the CEFC to allow for firming and grid support where there is market failure, IGCC does not support broader use of the CEFC for baseload gas projects, or any general support for the large-scale expansion of fossil fuel development as part of economic recovery policies. This is particularly the case as no analysis has been undertaken by the Government on the climate-related fiscal, economic and community risks associated with such policies.

IGCC would be happy to engage further with the Committee on the issues set out in this submission.

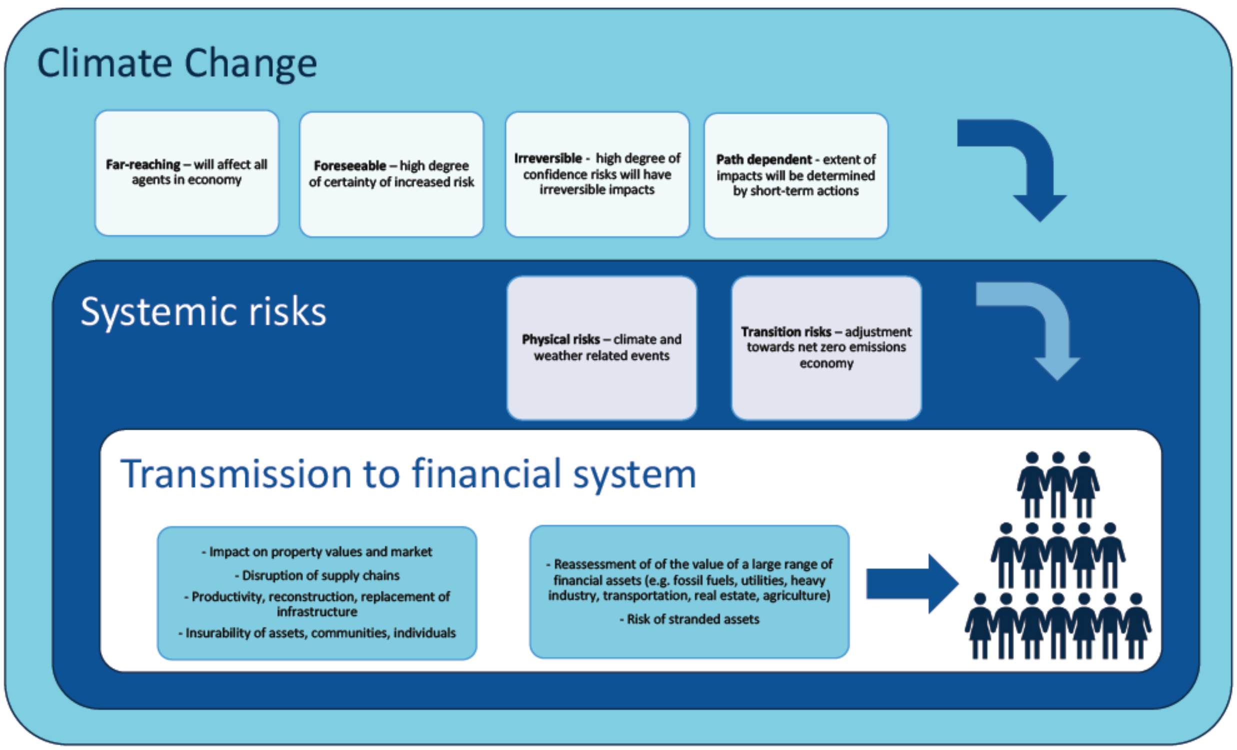
Introduction

The Investor Group on Climate Change (IGCC) welcomes the opportunity to make a submission to the Senate inquiry into the *Grid Reliability Fund Bill 2020* (GRF Bill). Institutional investors play a critical role in the long-term health of the economy and in the financial well being of millions of Australians. Globally, investors have trillions of dollars of capital to deploy towards climate change solutions if the policy settings to support this investment are right.

Climate change is a systemic risk to the financial system

Climate change is recognised as a systemic threat to the financial system, requiring thoughtful and prudent management (Figure 1). These risks have been acknowledged by financial regulators globally,[1] and climate change has been characterised in Australia as 'material, foreseeable and actionable',[2] requiring robust governance and risk management approaches from institutional investors.

Figure 1: Climate change and macroeconomic and financial stability*. Developed from Central Banks and Supervisors, Network for Greening the Financial System (2019)*[3]



Institutional investors have systemic exposure to climate change risks. A managed transition to net zero emissions and actions to build resilience to the impacts of climate change will reduce the cost of climate change and open up investment opportunities. Long-term investors have a critical role in delivering this more prosperous future and are increasingly changing their investment practices to align with a net zero emissions economy.

However, investors can't address climate change alone. Governments have an obligation to implement policies that are credible, durable and predictable. This will reduce financial risks and encourage investment in low and zero carbon opportunities. Governments can support private sector investment in new technologies by ensuring the enabling environments to large-scale investment exist and that the well-recognised barriers to institutional investment in zero and low emissions technologies are overcome.

The key policy priorities for institutional investors are establishing policy pathways to a net zero emissions by 2050, managing the energy sector transition and building resilience to climate-related risks in communities and economies.[4]

Overall comments on the Grid Reliability Fund

IGCC supports the overall policy objective of the Grid Reliability Fund. Greater investment in electricity distribution, transmission and storage is required to integrate large amounts of renewable energy and other zero emissions technologies into the energy system.

Specific Comments on the Grid Reliability Fund

Alignment with other Government policies

The transition of the energy system from high carbon to zero emissions has been coming for some time, is predictable and needs to accelerate if the goals of the Paris Agreement are to be achieved. To help manage this transition, investors support a policy approach which manages carbon, technology change and energy market considerations in an integrated manner.

A short-term and incremental approach to climate and energy policy development risks locking countries into inefficient and costly policy outcomes. Long-term, durable and market-based policy design can enable deep emissions reductions, a steady economic transition and open up new investment opportunities in Australia.

Policies that credibly support achieving the Paris Agreement's goals will provide the private sector with greater certainty as to the rate and pace of change. A clear pathway to transition will, in turn, improve investors' ability to assess climate-related risks and opportunities, to measure and disclose portfolio exposure to the low carbon transition, and to further invest in opportunities to support the transition to a zero carbon, climate resilient world.

The Government must embed the changes to the CEFC in a strategy to achieve net zero emissions by 2050 if it wants to unlock institutional capital in a broad range of low emissions technologies on the scale required.

In addition to changes the government has also made a number of other announcements that will impact on the operation of the GRF Bill. These include but are not limited to recent announcements to expand the mandates of the CEFC and ARENA, the Low Emissions Technology Statement, the Technology Investment Roadmap, new climate change resilience measures and the development of Australia Long-Term Strategy under the Paris Agreement.

We encourage the Government and the parliament to examine the GRF Bill in the context of these other policies as they will have a material impact on the success of the CEFC in unlocking private sector investment. For example, legislative changes to the CEFC's mandate should be examined alongside examination of the GRF Bill to ensure a coherent package of measures.

Specifically, the Government should:

- **Expand the CEFC's mandate to include developing financing solutions for adaptation**: Private capital will be critical to building resilience to climate change impacts as governments are likely to be fiscally constrained for some time due to the impacts of the COVID-19 pandemic.[5] The CEFC has been a significant investor in emissions reduction projects across Australia. Drawing on this experience of mitigation finance, several barriers to financing adaptation in Australia, such as insufficient project scale, lack of credible counter-parties and deriving a commercial investment return, could be overcome by extending the CEFC mandate to include adaptation and resilience projects.

Transparency on decision making criteria for low-emission technologies

The new, expanded definition of low-emission technology under the GRF Bill will mean, in a addition to the existing requirement, a technology is also a 'low-emission technology' provided the technology:

- Supports the achievement of low-emission energy systems in Australia; and
- Is for any of the following:
    - energy storage;
    - electricity generation, transmission or distribution;
    - electricity grid stabilisation

However, the GRF Bill does not define 'low-emission energy systems in Australia' and there is currently no transparency on how the criterion 'supports the achievement of low-emission energy systems in Australia' would be assessed.

Therefore, we recommend that further transparency on CEFC's criteria for a 'low-emission energy systems in Australia' is provided, and that it must be consistent with the Paris Agreement objective of achieving net zero emissions by 2050. The CEFC should publish criteria for 'a low emissions electricity system' to provide further transparency and ensure the CEFC satisfies itself that the investment's emissions profile is in line with the longer-term policy goals and the objectives of the Paris Agreement. For example, is the investment robust under the 'Step Change scenario' in AEMO's 2020 Integrated System Plan.[6]

The role of gas

There has been significant political discussion in Australia as to the role of gas infrastructure investment in support of the economic recovery from COVID-19. The extraction, transportation and use of gas produces significant amounts of greenhouse gas emissions. From a long-term investor's point of view gas carries the same types of climate risk as any other fossil fuel. Changes in climate policies, technologies or market sentiment can prompt the reassessment of the value of a large range of assets particularly in the energy sector.

When making decisions on emissions intensive gas infrastructure that has an operational life of several decades, investors must consider the risk that the asset will become stranded as climate policies are tightened over time and the economics of zero emissions energy production continues to undermine the financial viability of fossil fuels. As a result, global capital markets will increasingly scrutinise the climate risks associated with gas, leading to preferential investment in true zero emissions alternatives. This will be the case even if CCS is applied to the technology. The additional costs associated with the capture, transportation and storage of carbon dioxide make these technologies even less economic compared to other low emissions options.

While IGCC supports the changes to the CEFC to allow for firming and grid support where there is market failure, IGCC does not support broader use of the CEFC for baseload gas projects, or any general support for the large-scale expansion of fossil fuel development as part of economic recovery policies.[7] This is particularly the case as no analysis has been undertaken by the Government on the climate-related fiscal, economic and community risks associated with such policies. Government portfolio and investment decisions should be subject to climate risk analysis and disclosure in line with emerging practice in the private sector and among financial regulators such as Australian Prudential Regulation Authority and the Reserve Bank of Australia.

Expanded functions of the CEFC

The GRF Bill expands the CEFC's functions to further include:

> "at the request of a responsible Minister, to assist Commonwealth agencies in the development or implementation of policies or programs relating to supporting the reliability of energy grids"

In principle this is an appropriate expansion of the CEFC's function and will allow the Government's broader policy suite to include greater financial sector expertise in how the government policies can be rolled out.

Conclusion

IGCC supports the overall policy objective of the Grid Reliability Fund. Greater investment in electricity distribution, transmission and storage is required to integrate large amounts of renewable energy and other zero emissions technologies into the energy system. Leveraging private sector capital will be critical to delivering on the Government's stated goals.

Investors want to support low and zero carbon solutions. Awareness of the need to tackle climate risk across the portfolio and heightened appetite for exposure to emerging solutions are driving strong and growing investor appetite for climate solutions and clean technologies. However, these investments must also deliver sustainable risk adjusted returns and are not without their difficulties.

The Government must embed the Grid Reliability Fund and other changes to the CEFC in a strategy to achieve net zero emissions by 2050 if it wants to unlock institutional capital in a broad range of low emissions technologies on the scale required.

Finally, as governments implement their economic recovery plans from the COVID-19 pandemic, governments should prioritise sustainability and equity, and accelerate the transition to a net zero emissions economy to mitigate climate risk, create new jobs and catalyse the sustainable deployment of private capital. Recovery plans that exacerbate climate change would expose investors and national economies to escalating financial, health and social risks in the coming years. Governments should avoid the prioritisation of risky, short-term emissions-intensive projects.

IGCC would be happy to engage further with the Committee on the issues set out in this submission.

[1] NGFS (2019): https://www.ngfs.net/en/technical-supplement-first-ngfs-comprehensive-report

[2] Summerhayes (2017): https://www.apra.gov.au/news-and-publications/australias-new-horizon-climate-change-challenges-and-prudential-risk

[3] NGFS (2019): https://www.ngfs.net/en/technical-supplement-first-ngfs-comprehensive-report

[4] IGCC (2019:" https://igcc.org.au/investors-set-out-policy-priorities-to-limit-systemic-climate-risks/

[5] IGCC (2020): https://igcc.org.au/wp-content/uploads/2020/06/IGCC-submission-Bushfire-RC_30.04.20-final.pdf

[6] AEMO (2020): https://aemo.com.au/energy-systems/major-publications/integrated-system-plan-isp/2020-integrated-system-plan-isp

[7] Investor Agenda (2020): http://theinvestoragenda.org/wp-content/uploads/2020/05/THE_INVESTOR_AGENDA_A_SUSTAINABLE_RECOVERY_FROM_COVID-19.pdf