

Ms. Anthea Harris  
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By email to [submissions@climatechangeauthority.gov.au](mailto:submissions@climatechangeauthority.gov.au)

Friday, 14 September 2012

Dear Ms. Harris,

**Submission to review of the Renewable Energy Target scheme**

Enclosed is our submission to the abovementioned review. We encourage you to consider the recommendations we have reached and would be happy to discuss this with you in person.

Should you have any enquiries regarding this matter please do not hesitate to contact myself on [REDACTED] or Greg Hannan on [REDACTED].

Yours sincerely,



Stephen Orr  
Director Strategy and Regulation  
IPR-GDF SUEZ Australia

**IPR - GDF SUEZ Australia**

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# **Submission to the Climate Change Commission Renewable Energy Target Review**

14 September 2012

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# 1 Executive Summary

International Power-GDF SUEZ Australia (IPR-GDFS) recognises that ensuring policy settings are appropriate for current and future conditions, while still providing the stable legislative and regulatory framework that is imperative to attract and provide reasonable certainty to the necessary investment in large scale capital intensive power generation infrastructure (renewable or otherwise), presents a policy challenge.

Over \$6 billion has been invested to date in renewable generation, and in making those commitments, investors (both Australian and international) have relied on the Renewable Energy Target (RET) legislation remaining in effect.

In the same way that the Clean Energy Future package undermined investments made in good faith in Australian energy, dramatic changes to renewable energy in Australia have the potential to raise sovereign risk concerns for investors.

For this reason alone, in order to protect investments made under the various RET legislation, IPR-GDFS recommends that the RET continue to operate until 2030.

However, in light of passage of the Clean Energy Future legislation and other developments related to renewable energy policy in Australia (see Section 4.1), IPR-GDFS believes that it is timely for the Climate Change Authority to recommend a number of changes to policy settings related to the overall RET framework.

IPR-GDFS argues for the following changes to policy settings to result from the review of the RET:

- Following the elimination of multiplying factors that have distorted the supply of small scale renewable generation certificates, re-combining the large scale and small scale renewable energy schemes into a single market-based RET scheme that does not discriminate across technologies.
- Reducing the overall renewable energy target by levelling off the current trajectory for large scale and small scale renewable generation to reflect the impacts of changes in demand and carbon legislation, while not impairing existing projects or projects for which finance, approvals and contracts are in place for construction.
- Maintaining this modified trajectory to 2030 to ensure that existing projects are not harmed financially.
- Preventing publically funded organisations such as the CEFC and ARENA from being able to finance renewable projects and participate in the RET to avoid further market distortion.

## 2 About International Power-GDF SUEZ Australia

International Power, now a wholly-owned subsidiary of GDF SUEZ, is a leading independent electricity generating company with 75,579MW gross (43,288MW net) in operation and a significant program of 12,820MW gross (5,868MW net) projects under construction as at 31 December 2011. International Power is present in 30 countries across six regions worldwide. Together with power generation, International Power is also active in closely linked businesses including downstream LNG, gas distribution, desalination and retail.

In 2005, International Power Australia commissioned the Canunda wind farm, near Millicent in South Australia's south east, which was the first wind farm for International Power globally.

International Power entered the Australian energy industry in 1996 and has grown to become one of the country's largest private energy generators, with assets in Victoria, South Australia and Western Australia. The International Power portfolio also includes Simply Energy, a wholly-owned subsidiary of International Power and one of the larger second tier retailers operating in South Australia, Victoria and other National Electricity Market (NEM) regions.

## 3 Policy principles

IPR-GDFS, including Simply Energy, has actively engaged with the Federal Government on the design and implementation of greenhouse gas abatement and renewable energy policy, and now welcomes the opportunity to comment on the Renewable Energy Target Review (RET) issues paper released by the Climate Change Authority (Authority).

The current review of the RET is broad-ranging and focusses on detailed implementation issues as well as issues related to the role, need and design of the RET. We offer perspectives across this full policy spectrum.

Our arguments are based on adherence to the following policy principles:

- A stable regulatory and legislative environment that underpins investor confidence in large scale capital intensive infrastructure whether, it be renewable generation or fossil-fired generation.
- Policies which to the greatest extent possible rely on market-based mechanisms.
- Transparent objectives from Government in relation to climate change and energy policy.
- Avoiding the distortionary impacts of subsidies to particular technologies on the investment environment or "picking winners."
- Where changes to policy settings occur, that these must not be retrospective and that sufficient grandfathering provisions are in place to protect investments made in good faith under earlier regulatory and legislative frameworks.

## 4 General

As discussed in the issues paper the objectives of *The Renewable Energy (Electricity) Act 2000 (Cth) (REE Act)* are to:

- Encourage the additional generation of electricity from renewable sources;
- To reduce emissions of greenhouse gases in the electricity sector; and
- To ensure the renewable energy sources are ecologically sustainable.

IPR-GDFS notes that the review being conducted by the Authority must be consistent with the objectives of the *REE Act*.

Coupling the policy objectives of greenhouse gas abatement and deployment of renewables together is problematic. With a legislated carbon price now in place this problem is compounded. From the perspective of economic efficiency, least cost greenhouse abatement should be driven only by the price on carbon. If renewables are competitive and produce the lowest cost outcomes for consumers, then they will be built.

Even with a legislated carbon price, renewable deployment still remains contingent on the subsidies provided through the RET. Government must be aware that while the RET relies on market mechanisms, it primarily relies on a mandated target to deploy renewables. In the context of the suppressed demand growth currently being seen in Australia, forcing renewables into the market suppresses spot market prices, erodes the viability of incumbent generators of all types, and undermines investment certainty in merchant generation that is non-subsidised and market facing.

The original unbundled RET drove the deployment of large volumes of on-shore wind generation until further incentives were given to other forms of technologies, mainly rooftop photovoltaic (PV) cells. The distortionary use of multipliers and external grants for solar schemes resulted in a large increase in deployment of rooftop solar. This prompted a policy correction (to compensate for the impacts of the policy distortion) through the decoupling of large scale and small scale renewable schemes.

We highlight this to remind policy makers that active intervention in markets has a long track record of failure. The inconvenient truth of renewable policy is that renewables do not currently represent least cost greenhouse abatement at current global carbon prices, nor are they the new entrant generator of choice on an economic basis. This issue is increasingly being recognised globally in debates about renewables. For example, Dieter Helm, Professor of Energy Policy at Oxford University and Fellow in Economics at New College, Oxford recently illustrated this point in the context of UK energy and renewable policy<sup>1</sup>.

If we accept that the RET does satisfy the policy objective of renewable deployment, this then raises questions about its interaction with carbon pricing policies, and also its direct consequences for the sustainability of a competitive national electricity market.

Renewable policy in Australia and in other jurisdictions has been highlighted by cycles of boom and bust. Booms occur when governments use subsidies to “pick winners” and busts occur when these same subsidies become unaffordable for either governments or the public at large. To avoid repeating these mistakes, the Australian Government must be open and transparent about its methods and objectives in relation to renewable policy. There are difficult choices to be made, but it is better if these decisions once made are left to run their course and are not continually adjusted.

Our long held view is that the RET adds significantly to the cost of electricity for Australian consumers. In addition we have argued that mandated new generation is market distorting and increases the cost of emission abatement in Australia, while distorting signals in the wholesale electricity market.

These arguments have been vindicated as time has passed and evidence is collected on the impact of the RET on the electricity market and households. State and Federal agencies such as the Department of Resources, Energy and Tourism (DRET), The Australian Energy Market Commission (AEMC) and the Independent Pricing and Regulatory Tribunal of New

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<sup>1</sup> See [http://www.dieterhelm.co.uk/sites/default/files/Huhne\\_hype\\_060212.pdf](http://www.dieterhelm.co.uk/sites/default/files/Huhne_hype_060212.pdf)

South Wales (IPART) have provided a large body of contemporary evidence on the cost impact of the RET.

Typically these reports have estimated the relative contribution the RET has made to electricity price rises incrementally and therefore masking the cumulative impact. IPR-GDFS encourages the Authority to review this policy evidence in its own right but to also consider the cumulative impact that the RET has had in relation to household electricity bills since the policy was implemented.

We encourage the Authority to recognise these lessons of the past when recommending policy settings for the future.

### **RECOMMENDATION**

That the Authority as part of its discussion paper due in October 2012 consider the cumulative impact on electricity bills that the RET has had since 2001.

The decision to split the RET into large scale and small scale scheme has significantly compounded the problem of cost to households (and in particular the uncapped nature of the small scale scheme). The SRES has directly subsidised the take up of roof top solar PV panels which is both a costly and relatively inefficient form of greenhouse gas abatement. IPR-GDFS Australia appreciates the comprehensive list of issues contemplated in the issues paper. We offer responses to many of the themes raised in the paper below.

## **4.1 Relevant factors for the review**

The Authority's review, while required under legislation, occurs at a time of heightened sensitivity around issues related to electricity and specifically the cost of electricity in Australia. The following factors set the scene for the Authority's decision:

- Falling energy demand which has led to overcapacity in the NEM and low spot and wholesale contract prices.
- Ongoing public debate regarding the future level of the RET and costs associated with the policy.
- Continuing household and media focus on "cost of living" pressures to which electricity prices are a significant contributor.
- Recognition that State and Federal government renewable energy and greenhouse policies are contributing to electricity price rises.
- Formation of new Federal agencies such as the Clean Energy Finance Corporation (CEFC) and the Australian Renewable Energy Agency (ARENA).
- The failure of the RET to secure renewable energy manufacturing (short of construction) and thus has failed to deliver sustainable "green" jobs in Australia.
- International and national developments in relation to the gas reserves such as coal seam methane developments in New South Wales and Queensland and shale gas development in the United States, which are making gas more abundant and less expensive.
- Findings from bodies such as the Productivity Commission that while renewables subsidies have created jobs in the renewables sector, these jobs are likely to have come

at the expense of jobs in other parts of electricity generation and the economy more broadly.<sup>2</sup>

## 5 High-level position on the RET

IPR-GDFS is not opposed to renewables *per se* and has already invested in renewable generation in Australia at Canunda in South Australia.

However, in the current low demand growth environment, IPR-GDFS has strong reservations about the prospect of 41TWh of large scale renewables and at least 4TWh of small scale renewables being deployed in Australia.

While IPR-GDFS considers the RET to be a high cost policy, and unnecessary given the introduction of the Clean Energy Future legislation, it considers that continual alteration of policy settings in the long run undermines regulatory certainty and continues the cycle of sovereign risk for investors in Australia. For its part IPR-GDFS has invested in renewables on the basis of the RET settings at the time of investment.

IPR-GDFS recommends the following RET policy settings:

- Establishing a single market-based RET that does not discriminate across technologies.
- Maintaining a fixed energy target (in GWh) for renewables.
- Reducing the overall renewable energy target by levelling off the current trajectory for large scale and small scale renewable generation to reflect the impacts of changes in demand and carbon legislation, while not impairing existing projects or projects for which finance, approvals and contracts are in place for construction.
- Maintaining the levelled off trajectory to 2030 to ensure that existing projects are not harmed financially.
- Eliminating distortions through the use of multiplying factors.
- Preventing publically funded organisations such as the CEFC and ARENA from being able to finance renewable projects and participate in the RET to avoid further market distortion - unless there is a demonstrated market failure such that the revised overall target is at risk of not being met.

## 6 A single renewable energy target

It is the strong preference of IPR-GDFS that Australia return to a single renewable energy target. We strongly support the elimination of all solar credit multipliers from 1 July 2013 and believe this creates the opportunity for the Authority to recommend that the LRET and SRES be collapsed back into a single scheme. Having a single scheme aligns with the original policy intent of the Mandatory Renewable Energy Target (MRET) established in 2001, and absent the multipliers, there appears to be no sound basis for maintaining the size distinction.

A recurring problem in renewable policy design relates to incentivising renewable technologies which have different qualities and costs. Under a market-based scheme such as the LRET, investors work their way “up the cost curve” until the required demand level is reached. While policies such as this impact on existing generators, they allow targets to be reached in an economically rational manner.

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<sup>2</sup> See Productivity Commission report “Carbon emission policies in key economies. Supplement to the research report,” December 2011.

The original RET was a single scheme that did not discriminate between large and small scale renewable technologies. The introduction of solar multipliers created discrimination and led to preferential treatment of small scale renewables over large scale renewables. The use of solar multipliers was an example of how a technology neutral policy mechanism was distorted and created an over-supply of renewable energy certificates (RECs) which distorted the market. The large scale renewable sector is still suffering from this policy decision, three years later.

The separation of the LRET and SRES was a response to the distortion of the large scale renewable market that occurred as a result of small scale renewable deployment. It also reflected the different qualities that rooftop installations have compared to large scale installations such as wind farms.

However the decision to eliminate all solar multipliers now creates the opportunity for the SRES and the LRET to once again be combined into a single scheme. This would have a number of advantages for customers and the Government.

Firstly, the current design of the SRES represents an uncapped liability for retail customers because there is a payment for SRECs with no volume cap. This incentivises installers to roll out as many installations as they can. (This same uncapped liability issue has been confronted by State Governments who recognised that without volume limits, feed in tariff (FIT) schemes were financially unsustainable).

Secondly, the need for small-scale technologies to remain eligible for separate support under any renewable energy target is dissolving. These schemes were introduced to bring forward investment, by assisting with the upfront cost of purchasing small generators. This assistance is no longer necessary, as technology costs have rapidly reduced. Even with market-based FITs, the payback period of these systems is arguably becoming short enough to make the investment worthwhile for many households.

Australia has paid a premium for early entry of rooftop solar PV which could have been better spent more efficiently e.g. more panels later on and/or different technologies early on. The highest principle should be the least cost (risk adjusted) path be relied on to achieve the desired policy objectives.

The uncapped SRES increases the scheme liability beyond the original intended target. This increases the cost to consumers beyond what was originally accepted. It also means liable entities' individual targets are difficult to forecast. This risk also leads to increased cost imposed to customers. This is an inequitable outcome, because all customers face this impost through their electricity bills, cross subsidising those who are able to benefit from the scheme.

#### **RECOMMENDATION**

That the Authority recommends there be a single market-based renewable energy target in Australia which does not discriminate between small or large scale technologies.

## **7 The level of the renewable energy target (RET)**

IPR-GDFS recommends that the total target for renewables in Australia be reduced to recognise the distortionary impact that 45+TWh of renewable generation is having on electricity markets in Australia and the recent changes to electricity demand in Australia. It would also further erode market opportunities for non-subsidised investment in Australian electricity generation which threatens long term reliability of electricity supply.



IPR-GDFS supports maintaining a fixed energy target (in GWh) for renewables to provide investment certainty. Reducing the RET target by levelling off the current trajectory provides the opportunity to avoid impairment of existing projects or projects for which finance, approvals and contracts are in place for construction.

Any changes to the overall RET must be communicated to the marketplace well in advance of their implementation. While lowering the overall RET target would be a further example of Government policy revision, if done in an open, progressive and transparent manner and accompanied by sound justifications, investor confidence can be maintained.

Revising the target and an accompanying trajectory without impacting existing investors and then leaving this in place will provide investors and financiers with the highest confidence. Ensuring that the target and trajectory are also no longer affected by external distortions (such as occurred through solar multipliers) is also an essential precondition for maintaining investment and regulatory certainty.

If these transitional conditions cannot be met, the requirement for investment certainty is preeminent, and the RET target should be unchanged.

#### **RECOMMENDATION**

Reduce the overall RET but only if the change can be implemented in a way that does not undermine existing investments and projects for which contracts have been signed but construction has not yet commenced.

## 8 Small scale renewable energy scheme (SRES)

While our preference is for a single RET in the future (see section 6 above), IPR-GDFS has a number of comments in relation to the current design and administration of the SRES.

### 8.1 SRES administration (liability and surrender)

While the use of the Renewable Power Percentage (RPP) methodology is appropriate, the “ex-post” surrender targets which come at the end of the first quarter (31 March) in the liable year are not.

Retailers generally reassess their rates and cost-recovery model prior to the commencement of each liable year. Because the RPP is not released until the following March, retailers have to perform this modelling based on a forecast of their RPP for the coming compliance year. Retailers are then required to factor in an additional risk premium, in case the actual RPP is higher than the published RPP. This has the effect of increasing retailer risk premiums more than is necessary.

Setting an ex-ante RPP avoids creating unnecessary additional market risk. Since certificates are “bankable”, the RPP can be revised in future years to make up for any shortfalls or surpluses in surrendered certificates.

The logic of establishing the RPP in advance of the year of liability is relevant whether there is a separate SRES or where the SRES is rolled into an overall RET (as per our earlier arguments).

**RECOMMENDATION**

That the RPP be declared at the very latest by the start of the last quarter of the year preceding the year of liability, ie. changed from an ex-post target to ex-ante target.

## 8.2 Deeming

The issues paper asks if “deeming” is an appropriate way to provide certificates to SRES participants. In the view of IPR-GDFS, the use of deeming to provide certificates is excessively generous. The use of deeming is reasonable if the cost of metering is prohibitive or where metering is not available. This is not the case given that the installation of roof-top PV solar typically also requires a bi-directional (Type 4) meter to be installed

Reliance on deeming raises the risk that payments are made for certificates which may never actually be generated. For example, the uncapped nature of SRES encourages installers to compete for market share by maximising the up-front subsidy to customers. This typically is achieved via the 15-year deemed profile where a household transfers fifteen years of certificates to the installer on the day the rooftop PV solar panels are fixed to their roof. This creates an over-supply of SRES certificates and encourages cash-constrained installers to sell these certificates at a discount to the SRES certificate price cap of \$40.

There is also a real risk that installations do not operate for the life of the deemed profile, or at the nameplate capacity. This risk is heightened where installers have used cheaper and lower quality panels, inverters and other equipment. Since rooftop PV solar installations are exposed to the elements, there is a real risk that there will be equipment faults or progressive reduction in performance which result in significant discrepancies between deemed and actual output. In this instance, customers would literally be paid (by other consumers) for something which does not exist.

To address this issue, IPR-GDFS recommends that overly generous deeming provisions be replaced by a system which relies on testing and inspection of systems prior to SREC’s being issued for either a three or five period.

**RECOMMENDATION**

That the use of deeming be reviewed and at a minimum, the use of 15-year deemed profiles be phased out.

That deeming is limited to either three or five years and that this is subject to mandatory testing and inspection of installations.

## 8.3 Eligible SRES technologies

IPR-GDFS does not support inclusion of displacement technologies into the SRES. To do so would create potential for dual subsidies from separate State and Federal Government schemes. It would also be a retrograde step given that the current design of LRET and SRES was in part influenced by a desire to rationalise a raft of disparate State-based schemes.

**RECOMMENDATION**

That SRES be limited to generation technologies and that displacement technologies continue to be excluded.

## 9 Interaction of the RET, CEFC and ARENA

IPR-GDFS has argued against the CEFC and ARENA acting as a competitor to private investors in the NEM and in Australia generally. Our preference is that these organisations, if they exist at all, focus on funding research and development, and avoid substitution or distortion of commercial processes.

The CEFC is a body which gives licence to Government to “pick winners” and erode genuine market dynamics. The CEFC should not be able to finance a renewable project which also receives renewable energy certificates. To allow otherwise gives projects funded by the CEFC advantageous competitive positions against the free market. This in turn would make un-subsidised “stand-alone” investments less viable.

To prevent crowding out of private investment, organisations such as the CEFC and ARENA should not be eligible to participate in the RET.

### **RECOMMENDATION**

That the CEFC and ARENA not be eligible to participate in the RET.

## 10 Diversity of renewables

The issues paper raises questions about the diversity of renewable deployment in Australia. With separate large scale and small scale schemes, the Government created a mechanism for two classes of renewable generation to be deployed.

The market in small and large scale renewables is largely deploying onshore wind generation and rooftop solar panels. Neither of these technologies can any longer be considered “new”; both have seen significant cost reductions and technology innovation over the last decade.

We regard creating greater renewable diversity as “code” for greater market distortion and “picking winners” which are higher up the cost curve. The integrity of the RET scheme has previously been undermined by earlier actions to sponsor diversity.

IPR-GDFS encourages the Government to rely on market forces to deliver the most economically efficient renewable technologies. To do otherwise will lead to higher costs to electricity customers and create a further episode of boom and bust in renewable policy, centred around a new technology category.

It is not possible to maintain the integrity of a RET scheme by allowing different technologies to receive different levels of subsidy. Diversity should be driven by market mechanisms in a stable regulatory environment where the different technologies compete on an equal footing.

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