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Dear Mr Archer

SUBMISSION TO THE RENEWABLE ENERGY TARGET REVIEW

The Australian Industry Group welcomes the opportunity to provide a submission to the Review of the Renewable Energy Target. Our detailed comments on the matters raised in the Issues Paper are at the **Annexure**.

We look forward to further opportunities to provide input on the Review's evolving proposals.

For any questions about this submission, the appropriate contact is Tennant Reed (03 9867 0145, tennant.reed@aigroup.asn.au).

Yours sincerely,

A handwritten signature in blue ink that reads 'Innes Willox'.

Innes Willox
Chief Executive

AUSTRALIAN INDUSTRY GROUP SUBMISSION TO THE 2014 REVIEW OF THE RENEWABLE ENERGY TARGET

Introduction

The Australian Industry Group welcomes the opportunity to provide a submission to the 2014 Renewable Energy Target (RET) Review.

Our membership is broad and diverse and includes a wide range of more- and less-intensive energy users; makers of equipment and providers of services for use in renewable and non-renewable energy systems; and electricity generators of all kinds. These businesses are all affected by the RET in different ways, and we have benefitted from their input and expertise in preparing our response to the Review Panel.

The diversity of our membership is reflected in the different positions held by our members regarding the RET. While the large majority of our members have no firm view on the RET, some are strongly opposed to it. They view it as an unnecessarily expensive and ineffective policy and would like to see it abolished or significantly scaled back. Others argue that the RET plays an important role in helping to transform our electricity generation mix to cleaner and more diverse sources, in addition to supporting growth and employment in the renewable energy sector. This group views the RET as being important to Australia's future energy security and economic base and are advocating that current targets be maintained or even strengthened.

Despite the disparity of positions in our membership regarding the RET, their positions are nearly always underpinned by the same overarching concerns: that future energy is affordable and secure, and that climate and energy policy is stable, predictable and credible, and minimises the potential for sovereign risk. These concerns are critical to informing Ai Group's position on the RET, and we believe they should be essential components of any consideration of climate and energy policy. With these points in mind, we dedicate the remainder of this submission to the following issues:

1. the level and duration of the Large-scale Renewable Energy Target (LRET);
2. the Small-scale Renewable Energy Scheme (SRES), its ongoing contribution to the RET and opportunities to ensure that costs of the SRES are contained within reasonable limits;
3. other reforms to the RET that are required to improve its efficiency and effectiveness; and
4. other policies (at all levels of government) that affect the costs and benefits of the RET.

1. Level and Duration of the LRET

Ai Group opposed the expansion of the RET in 2009, on the basis that it was not the most efficient policy to drive emissions reductions or low-emissions innovation. The expansion nonetheless went ahead with bipartisan support, leading to substantial additional investment in large- and small-scale renewables. This reality required reassessment. In 2012, in our submission to the Climate Change Authority's review of the RET, we argued that at that time, it was not practical to remove the scheme and it was not clear that there would be a net consumer benefit to significant reductions in the LRET short of removal. We suggested the better approach was to pursue steps within the existing RET framework to reduce costs without compromising investment and policy certainty and suggested that measures to contain the costs of the RET to trade exposed industry should be maintained, streamlined and strengthened.

We maintain strong concerns about the lack of certainty surrounding climate and energy policy and its impacts on investment. However, it is prudent that we review our position in light of the current policy and economic environment. More specifically, our 2014 RET position considers the following four factors which are contributing to policy and economic uncertainty in Australia:

1. The sustained period of particularly difficult trading conditions for many, in part the consequence of rising energy costs.
2. The uncertain nature of climate and energy policy in Australia, including the likely removal of the carbon tax; uncertainty regarding the detail, implementation and impact of the Government's proposed Emissions Reduction Fund (ERF); and uncertainty surrounding the future of existing and additional policies to support research into and deployment of new energy sources.
3. Falling demand and strong supply in the National Electricity Market (NEM) which, despite pressures on retail prices, have depressed wholesale prices and make the NEM very unlikely to drive substantial investment in large-scale electricity generation over the next decade.
4. Slower than expected investment in wind and other large scale renewables, initially because of an oversupply of certificates from small-scale technologies and more recently due to policy and political uncertainty.

Given this environment, it would be very difficult to accept any change to the RET that would impose net costs on business, and especially trade exposed businesses, or would diminish support for emissions intensive trade exposed businesses to meet their liabilities. In this respect, we consider the costs of either increasing the target or completely abolishing it to be unacceptably high. If the target were abolished industry would expect security for investments in renewable generation that have already been made, either through very substantial compensation via the Budget, or through an ongoing payment by electricity retailers, and ultimately energy users, in a closed, grandfathered version of the RET. Even a fully compensated abolition of the RET could have implications for risk and financing costs in the electricity sector.

Ai Group members have expressed concern that such an about-turn by the Commonwealth would have major implications for international investment in Australia due to perceptions of increased sovereign risk. These negative perceptions would have a lasting impact that might be as significant as any claims for compensation that arise from those who have invested in renewable energy. In addition, even if compensation were provided, the abolition of the RET would have serious implications for manufacturers, vendors and installers of small-scale solar PV and solar hot water, unless publicly funded rebates for these technologies were re-instituted.

The environmental and social implications of the RET also need to be considered. The RET is not the most efficient tool for reducing emissions, since it is narrowly focussed on one set of technologies in Australia's energy generation sector. However, the RET has fostered the growth of the renewables sector and led to significant greenhouse gas abatement in Australia. If the RET were removed or significantly scaled back, there would be a much larger gap between likely emissions and Australia's commitment to reduce greenhouse gas emissions to at least five per cent below 2000 levels by 2020. The cost and difficulty of bridging this gap through other policies could be significant, particularly if low-cost international abatement options are excluded.

Renewable generation will undoubtedly play a major role in Australia's future energy system and in the long-term transition to a low-emissions economy. However, with investment in large scale renewables held back in the last couple of years by policy upheaval and uncertainty, it now appears difficult, and potentially impractical, to approve, construct and commission sufficient new capacity to hit the 41,000 GWh target in 2020 - just six years away – within the current policy parameters. Meeting the existing target would require a mammoth construction effort in a short period, mobilising substantial resources and swiftly navigating State and local planning while maintaining standards. Costs would likely rise, driving certificate prices towards the ceiling and risking a situation where penalties are paid without drawing in new generation.

If the current 2020 target were delivered without hitting the ceiling price, this effort would most likely be rewarded by a swift and severe contraction in investment as the LRET plateaus between 2020 and 2030. In short, a rapid growth period, characterised by an increase in investment and consumption, will be followed by a prolonged drought in investment. This boom-bust investment cycle would entail job losses, unnecessary disruption and a high risk of capital being underutilised. While Australia would see a sharp increase in renewable generation capacity, long-term gains are unlikely to be any higher than those achieved by a more sustainable investment pathway.

In summary, no one would benefit from having a target that cannot be practically achieved by 2020; not the renewables sector, not energy users – who will have to fund the effort, not the community and not government.

These issues raise the question about whether our previous stance on the RET remains appropriate or whether it needs to be reconsidered. For most of our members this question is best answered by considering the net effect of the RET or proposed changes to it on their energy costs. Ideally, our answer to this question would be informed by the outcomes of the

Government's latest RET modelling exercise. However, a number of studies^{1,2,3,4} exist that investigate costs of the RET and likely changes to it, and these all point to the one conclusion: that, given the widely corroborated effect of the RET in lowering wholesale prices, significant reductions in the RET would deliver mediocre or negative benefits to energy users. This is not true of reductions aimed at deliverability, since generation that is not ultimately built cannot lower wholesale energy prices. **On that basis we suggest that, unless strong evidence to the contrary emerges, the large-scale RET target should be lowered to a level that is practically deliverable in 2020, but no further.** By 'practically deliverable' we mean a target that will not result in a boom and bust cycle of investment, with risks to employment, energy security, the supply of raw materials and potentially breaches of environmental and safety standards. We strongly encourage the Government to work with the renewable energy industry and suppliers to it to determine a target that can be practically delivered by 2020.

Beyond 2020 it is very difficult to comment on the most sensible approach to the LRET. The Australian Energy Technology Assessment (AETA) projections⁵ highlight the growing competitiveness of large-scale renewable technologies compared to other new builds. In particular, new wind builds are projected to be cost competitive with new fossil fuel generation capacity by 2020. The price of solar technologies is also projected to come well down the cost curve. As such, the need for policies to support investment in renewable generation may well be diminished, depending on future emissions reduction ambition. Climate policy can also incentivise investments in renewables by improving their relative cost competitiveness, whether through carbon prices, abatement prices, or regulatory requirements. Wider climate policy was previously expected to effectively phase out the RET over time.

Given uncertainty regarding future climate policy and the relative costs of renewable technologies, **we recommend the LRET be capped at a level that is practically deliverable in 2020, and that questions of any further increases to the level of the target, and its potential duration past 2030, be considered in the context of a comprehensive, consultative and apolitical review of post-2020 climate and energy policy.**

As we get closer to 2020 it will become increasingly more urgent to make a decision on the future of the LRET beyond 2030 and on any increases to the target beyond 2020 levels. These matters should be addressed at, or before, the 2018 RET Review. We would be concerned that industry would have insufficient time to prepare for scheme changes should details of the future of the LRET be finalised after this time. If a decision is made to raise the post-2020 level of the LRET it may be necessary to extend the scheme beyond 2030, since

¹ Cludis, J.; Forrest, S.; MacGill, I. 2013: Distributional effects of the Australian Renewable Energy Target (RET) through wholesale and retail electricity price impacts. Australian School of Business Research Paper No. 2013 ECON 33, University of New South Wales. Available at:

http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2359205

² Gerardi, W. & Nidras, P. 2013: Estimating the Impact of the RET on Retail Prices. Final Report. Sinclair Knight Merz, June 2013

³ Noort, J.; Vanderzalm, S.; Morris, B.; Zembrodt, L. 2014: Australia's Large Scale Renewable Energy Target: Three Consumer Benefits. Schneider Electric. Available at: <https://www.creativeenergy.com.au/>

⁴ Roam Consulting 2014: RET Policy Analysis. Report to the Clean Energy Council, 29 April 2014. Available at: <https://www.cleanenergycouncil.org.au/policy-advocacy/renewable-energy-target/ret-policy-analysis.html>

⁵ AETA: 2013 update, available at: <http://www.bree.gov.au/publications/australian-energy-technology-assessments>

at least ten years of scheme revenue are likely to be needed to give sufficient certainty to renewable generators to invest.

The above recommendations are made in light of the currently available evidence on likely future impacts of the LRET, particularly on energy users. Should the Review reach a different view on the basis of further evidence, then we would expect that industry would be consulted on the evidence and proposed changes to the target. If, following this consultation, a recommendation was made that the LRET be abolished or substantially reduced, then industry would expect steps to smooth a transition to the amended policy. At the very least this would include forewarning to allow industry time to prepare for major scheme changes that are being seriously considered by the Government, and security for investments in renewable generation that have already been made. The costs of such security should be taken into account in considering net impacts on energy users and taxpayers.

2. The contribution of the SRES to the RET

The separation of the LRET and the SRES provided greater certainty for investment in large-scale renewable technologies, uptake of which was threatened in 2009-10 by the confluence of falling costs and multiple generous subsidies that boosted demand for small scale technologies within the former unified market. However, this decision saw an unacceptably high spike in costs of the RET for energy users in 2011-12 as a result of intense activity under the SRES. Subsequent policy responses⁶ have greatly reduced SRES costs from the peaks of 2011 and 2012. These developments indicate that costs of the SRES to energy users can be appropriately managed and there is little benefit, and potential risks, to re-merging the two schemes.

Ai Group does, however, remain concerned at the potential for the level of support for solar photovoltaic (PV) systems to again become significantly out of sync with the actual price of these technologies in the market. The widespread adoption of small-scale technologies in Australia – more than 1 million households in Australia have installed solar panels – and internationally, has both reflected and driven their increasing cost-competitiveness. Investments in small-scale solar PV remain strong as the price of this technology continues to fall and businesses and households look to reduce their exposure to rising electricity prices. As such, we feel it is important that support for solar PV is regularly and predictably adjusted in line with the technology's increasing competitiveness.

The previous RET Review proposed an approach of slowly reducing the deeming period for small-scale technologies. This approach was accepted the former Government, and would see support for these technologies reduce over time, and cease in 2030.

Another approach would be to reduce SRES support according to a formula, as opposed to a fixed timetable. The formula would need to take account of changes in the consumer cost of small scale technologies and in retail electricity prices. This would be more complex and somewhat less predictable – important matters in the last Review – but would also be more

⁶ Most states have substantially reduced or abolished feed-in tariffs for solar PV and SRES certificate multipliers for solar installations have been eliminated.

likely to produce well-calibrated levels of support. This could be done through changes to the deeming period or certificate price, or by applying a discount factor to the number of certificates issued.

Each of these alternatives are preferable to an approach of placing a cap on the SRES, as this could cause 'boom and bust' cycles of investment in small-scale technologies. Whatever method is used, any reduction of SRES support should be as predictable as possible and closely tied to actual improvements in competitiveness. Industry should be consulted on proposals to amend the SRES, and given adequate forewarning and time to prepare if major scheme changes are seriously considered by the Government.

Finally, eligibility for the SRES should not be extended to any new technologies until an appropriate process is put in place to prevent future spikes in small-scale technology investment.

3. Other reforms to the RET

Reducing the cost of the RET

Emissions intensive and trade exposed (EITE) industries have enormous difficulty in passing on costs and are often less able to benefit from wholesale price impacts of the RET. The assistance arrangements for these industries need to remain a core part of the RET. Those arrangements can also be improved. Previously we recommended steps be pursued within the existing RET framework to reduce its cost, including making Partial Exemption Certificates (PECs) more tradeable and fungible. PECs are not tradeable certificates and can only be used at present by liable entities. Problems have been created for both EITE businesses and retailers as a consequence of the negotiation process. These problems arise because there is an information asymmetry between retailers and customers on gross costs of the RET. The current approach also makes it more difficult for an EITE business to change energy retailer during a calendar year as PECs are issued in the current retailer's name for the whole of the year. PEC tradability would streamline the application process for EITE assistance under the RET by reducing the need for EITE businesses to negotiate the value of their PECs with their energy retailers.

While the former government accepted recommendations to allow opt-ins to the RET and make PECs tradeable, and consulted on much of this, little change was enacted before the election. Ai Group would like to see steps taken immediately to enact these changes.

Eligibility of different technologies

Ai Group is open to other technologies being included in the LRET, so long as the introduction of these technologies is managed in a consultative and transparent manner. Past experience has shown that new sources of renewable energy have the potential to greatly reduce energy retailers' costs in meeting their liabilities, so it is important that new sources of renewable energy are able to be evaluated for eligibility as they become available.

Obvious candidates include waste-to-energy applications, which have the potential to abate emissions, make better use of abundant and ongoing waste streams, and reduce demand for grid electricity in Australia. For example, some municipal and industrial waste streams, and wood waste from sustainably managed forests, could potentially make a strong contribution to renewable energy, and, in some instances, would help to encourage the collection and processing of waste that might otherwise rot in situ or be sent to landfill. However, we note that concerns have been raised in the European Union, the United States and elsewhere about the net benefits of some bioenergy policies and projects. These concerns arise where policy design or market factors drive unconsidered impacts on the environment and society through land use and commodity markets.

Bioenergy can overcome these concerns with good policy, management and engineering. However, it would be sensible to ensure a strong evidence base on the life cycle impacts of any additional large scale technologies in the Australian context before they are included in the scheme.

Subject to such assessment, expanding the list of eligible large-scale generation technologies is sensible. However Ai Group does not support changes to mandate diversity within the RET. The policy should remain as close to technology neutral as possible within its restricted scope. Other policies can more cost-effectively ensure that there is an appropriate level of diversity in Australia's renewable energy generation over time.

The frequency of RET reviews

While governments and Parliament always retain the power to alter policy, this prerogative needs to be exercised with care if policy is to have the credibility and stability that attracts investment and lowers costs. Ai Group recommends that, as a matter of policy, the Clean Energy Regulator release an annual data report on outcomes of the RET, and that deeper reviews of the RET policy are conducted no more frequently than once every four years. The purpose of data reports would be simply to monitor how the scheme is performing and to note the implications of changes in the broader policy environment to the RET scheme, including policies at the State and local government levels as far as practical. Findings of the data releases would feed into the deeper four yearly reviews, which would, barring extreme circumstances, be used as the forum for raising recommendations regarding amendments to the legislation underpinning the RET scheme. Smaller adjustments to the scheme in between reviews, such as reductions in support for small scale technologies in light of improvements in their competitiveness, should be as mechanical and predictable as possible.

If endorsed, this recommendation would mean the next major review of the RET would be held in 2018. As discussed above, we believe this review should either be part of, or take account of the outcomes of, a comprehensive, consultative and apolitical review of post-2020 climate and energy policy, including a discussion of the future of the RET post 2020.

Consequences of the self-generation exemption

Ai Group has concerns regarding what we believe is an unintended negative consequence of the wording of the self-generation exemption in the *Renewable Energy (Electricity) Act 2000* (the Act) on some of our members. A number of our members generate their own electricity and have transmission lines to transport this electricity to where it is needed. In some instances members have allowed various incidental and community service offtakes from their transmission lines. These offtakes enable valuable services to be provided to the local communities in which they are based. Those services may not otherwise be provided as the cost of investing in new infrastructure to secure their own, often very small requirement for electricity, would be prohibitively high. However, in order to qualify for the self-generation exemption, the Act requires that dedicated electricity lines be used solely for the purpose of transmitting electricity between the two sites. As a consequence, those businesses providing access for incidental and community service use are no longer exempt from these costs and need to purchase Renewable Energy Certificates for all the electricity carried on the dedicated line. There is a considerable cost to purchasing these certificates and, aside from disconnecting incidental users from their transmission lines, the only other option affected companies have is to bear these costs.

Ai Group seeks urgent amendment to the Act to allow for incidental electricity offtakes to provide community benefits in remote locations without disqualifying the resource project from the exemption. This was a recommendation arising from the CCA's 2012 RET Review, but was not actioned through legislative amendment prior to implementation of the caretaker period and the September 2013 election.

In addition, Ai Group requests an urgent review of the self-generator exemption to ensure that all self-generated electricity consumed by the owner of that generation falls under the application of the self-generator exemption. At present, there are businesses who are incurring a RET liability for electricity supplied to their own manufacturing plants where they are more than one kilometre away from all or part of their generation infrastructure. This is a particular concern for businesses with industrial co-generation.

4. Other policies (at all levels of government) that affect the costs and benefits of the RET

The RET needs to be considered in the context of broader energy policy, which should have the objective of delivering reliable and competitively priced energy and a stable and predictable policy environment to support investment in Australia's energy systems that is efficient in the long term. As such, we believe that the 2014 RET review should be developed in close consultation with other relevant reviews currently underway, including the Energy White Paper Review, Eastern Australia Gas Market Strategy to 2020 and Emissions Reduction Fund policy.

It is also vital to take into account other important energy policies at the State and Federal levels that have the potential to impact the effective and efficient functioning of the RET. In particular, some policies have the potential to unnecessarily raise costs and inhibit uptake of renewable energy in Australia. The impacts of these policies should be assessed and the Review should recommend that they are abolished or amended where the assessment is

unfavourable. One key example is restrictive planning laws in some States that effectively rule out the construction of wind turbines in areas that are ideal for that purpose. Energy policies should be supported by strong scientific evidence. Another important consideration is whether State feed in tariffs are set appropriately. Excessive feed in tariffs have previously led to unsustainable increases in the rate of take-up of uncapped small scale renewable technologies, with substantial costs to energy users.

Finally, the 2014 RET Review should consider the issue of tariff structures for electricity networks and their relationship to distributed energy, particularly solar energy. Approximately 1 million households have installed roof-top solar PV systems and some have argued that many of these households may implicitly receive a subsidy on their network costs from other power users. A solar PV household reduces its total demand for energy, but their peak demand will not necessarily reduce to the same degree, and they will still typically use the network at night. If charged for network usage on the basis of annual demand (volumetric pricing), such a household may reduce its payments by far more than its contribution to systemic costs. Thus the network cost burden could fall more heavily on those households and businesses without solar PV installations.

It should be noted that the widespread installation of air conditioners has made a major contribution to increasing network costs, and that volumetric pricing of network usage has subsidised this by failing to recognise the contribution of air conditioning to overall network costs through increasing peak demand. It would be inequitable and inefficient to penalise solar owners without similar treatment for householders with air conditioning. In some instances the installation of solar PV systems may reduce the need for network augmentation, particularly in new developments and areas of strong growth. In some others, PV could actually increase network costs because infrastructure upgrades may be required to accommodate the flow of electricity from solar systems back onto the network.

If simple volumetric network pricing remains, as more and more people install solar systems, network costs will fall on smaller quantities of electricity consumption, stimulating further investment in solar technologies as people look to reduce their exposure to rising electricity prices. A shift towards fixed network connection charges would damage incentives to efficiently use the network, and would encourage energy users to secede from the network entirely – particularly if and when energy storage options become more cost effective. These so-called ‘death spiral’ scenarios can be exacerbated if government subsidies for solar PV are excessive relative to falling costs. By contrast, charging for network use based on peak demand and time of use would encourage fairer, more efficient and more sustainable outcomes. However, such systems will be more complex and need careful introduction and development. The current RET Review is unlikely to resolve these issues, but should be an opportunity to advance the public debate.