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Committee Secretary
Senate Standing Committee on Environment, Communications and the Arts
PO Box 6100
Parliament House
Canberra ACT 2600
Australia

21 May 2010

Dear Committee Secretary

Submission on the Renewable Energy (Electricity) Amendment Bill 2010

Thank you for the opportunity to submit Rheem's views on the above legislation. As the largest appliance manufacturer in Australia, the employer of over 1300 Australians and a major supplier of products that are eligible under the RET scheme, we believe that we have some insights and thoughts that may be valuable in your deliberations.

Firstly Rheem would like to state that we welcome the Government's ongoing support for the uptake of renewable energy products that is currently provided by the RET Scheme.

We also believe that it is important to state at the outset that Rheem does not view (nor wants to view) the trading of RECs as an opportunity to make a profit. Our business is the manufacture and sale of water heaters. The trading of RECs is a forced by-product of this activity. Whilst the administration of RECs adds to our cost base, we view this as necessary to enable the quick redemption of RECs by the householder. Our comments on the operation of the scheme should therefore be taken in the spirit with which they are offered – not as a way of maximising the value to us of RECs - but as comments on the efficiency of the RET Scheme's operation.

Rheem's approach to the operation of the RET is that it is at its most effective when two criteria are met:

1. **The householder receives the value of the REC at the point of sale. This is critical as it helps the householder overcome the potential "sticker shock" of renewable products, and ensures they are not out of pocket whilst awaiting creation and sale of their RECs. Installers need almost immediate redemption of their RECs if they are to give immediate discounts to householders**

2. **A high proportion of the REC value can be passed to the householder. For installers and suppliers to offer a high proportion of the REC value to householders, their**

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administrative and holding costs need to be minimised. The higher the proportion, the lower the cost of installation to the householder, which in turn leads to greater uptake.

For these two criteria to be met, the scheme must operate in a way that encourages installers and suppliers to operate confidently in the market and pass on the maximum value of the REC to the householder. This means that the scheme's operation should, where possible, eliminate uncertainties regarding REC demand, future REC prices and cash flow. This approach was the basis of our April 2010 response to the Dept of Climate Change's discussion paper on the proposed RET changes. It is Rheem's belief that scheme now detailed in the proposed legislation before Parliament has not adequately addressed the key issues that Rheem raised in its original submission. The most notable examples where this uncertainty has not been addressed are:

- **A cap of a $40 per Small-scale Renewable Energy Scheme (SRES) REC will result in substantially lower householder REC prices**

  The majority of small scale installers offer the REC value as a discount at the point of sale. With a SRES price cap of $40, most installers will discount the REC price below this figure to ensure they are not operating at a loss should the REC price fall. Whilst this situation is similar to the operation of the current scheme, the proposed upside price cap means that losses on one job cannot be offset by profits on another.

  In the short term this operational flaw will push some less cautious installers from the market as their cash flow is impacted, whilst in the longer term it is likely that an overcautious approach to REC pricing will be adopted. This will result in considerably less of the REC price being passed on to householders, as installers protect themselves against market uncertainty.

  A potential solution to this issue may be the **implementation of a minimum SRES REC price** to complement the maximum price.

- **The SRES targets will be set annually, which is too infrequent to keep pace with the market.**

  Under the proposed regulations the regulator will set annual targets for SRES RECS, thus creating demand for these certificates. The regulator in setting these targets will be attempting to match targets to predicted SRES REC creation, so that a market equilibrium occurs at or about the cap price of $40. A surplus or shortfall of SRES RECs will occur when the actual installations vary from the target.

  Rheem believes that there is a high likelihood of an underestimation of SRES REC creation, given that some of the key drivers for small scale generation uptake are changes to state and federal environmental policies. For example, changes to the Federal Government's Solar Water Rebate scheme have reduced demand for heat pumps by 70% in the last 9 months. Similarly, the NSW Government's introduction of a gross feed in tariff for PV installations has substantially increased the uptake of solar PV. Neither of these changes could have been foreseen and therefore could not have been included in the annual target setting.

Assuming that these types of changes will continue to occur, the ability to accurately set SRES targets that match SRES installations would appear to be limited. Any underestimation of small scale installations will create a surplus of certificates. As the regulator is locked into annual target setting, the target cannot be changed until the following year, making it possible that a surplus of SRES RECs would not be cleared for up to nine months.

Without the ability to vary the SRES target on a more frequent basis than that currently proposed, it is possible that **an incorrectly estimated target could work as a de-facto cap on installations** – limiting installations by eliminating the demand for RECS.

Apart from the perverse outcome of discouraging uptake of renewable products, any cap, de-facto or otherwise, would also condemn installers and manufacturers to a boom-bust cycle where sales boomed for as long as the target is unmet and RECs can easily be sold, followed by potentially months of poor sales where RECs can't be offered as they can't be sold. This lack of continuity in the business cycle is not manageable and would cause considerable damage to the existing industry.

Very few, if any, installers and suppliers would be able to cope with the cash flow implications of this type of scenario. We would therefore recommend that **the regulator be given discretion to amend the SRES target on a more frequent basis than that currently proposed**, taking into account any significant changes in the drivers of the market and responding to the impact of these distortions as they occur.

- **The Clearing House Model could exacerbate cash flow issues, not resolve them**.

  Rheem's current understanding of the proposed SRES clearing house is that all creators of RECS can register their SRES RECs for sale through the Government's "clearing house", which will sell them to the market at the cap price of $40 (excl GST) on a "first in first out" basis. The proceeds of the sale will then be paid to the owner of the SRES REC.

  The main concern here is that any oversupply of SRES RECS may sit in the clearing house for up to 11 months (or more if the annual target is not revised sufficiently), until new targets are set for the following year. The only option for those with resulting difficulties would be to withdraw them from the clearing house and sell them on what is likely to be an extremely low priced "spot" market.

  Neither of these situations address the cash flow issue that the clearing house was presumably set up to avoid – cash flow difficulties for those needing to sell their RECs quickly at a price close to what they have already given as a point of sale discount.

  The suggestion above regarding more frequent reviews of the target would go some way to eliminating this as an impediment to the operation of the scheme. Our preferred solution would be for **the regulator to operate the clearing house as a "suspense account", paying out monthly for any SRES RECs registered, then repaying itself through the sale of these RECs** at a later date.

All of these issues go to the fundamental concern which Rheem has with the operation of the scheme as outlined in the current legislation – that it fails to facilitate the speedy sale of SRES RECs that are created through installations. If this occurs it is likely to force installers and suppliers to take a different path:

- eliminate point of sale REC offers
- offer heavily discounted REC prices to householders
- incur a heavy holding cost until new annual targets are set
- accept low bids from REC buyers looking to take advantage of cash flow constrained installers.

Rheem believes that our suggested amendments to the legislation would address these concerns. It would also ensure that the RET scheme operated to not only support the uptake of renewable technologies, but to alleviate the cash flow burden on installers and suppliers, many of which do not have the ability to survive mis-steps in policy and legislation.

I would welcome the opportunity to further expand on our views regarding this legislation if the Committee deems that this would be useful.

Yours sincerely

MATT SEXTON
CEO, RHEEM AUSTRALIA