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Committee Secretary
Senate Standing Committee on Environment, Communications and the Arts
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"Inquiry into the Renewable Energy (Electricity) Amendment Bill 2010, the Renewable Energy (Electricity) (Charge) Amendment Bill 2010 and the Renewable Energy (Electricity) (Small-scale Technology Shortfall Charge) Bill 2010"

TRUenergy welcomes the opportunity to provide the following comments on the 'Renewable Energy (Electricity) Amendment Bill 2010 and related bills' (the bills).

TRUenergy supports the direction and intention of the policy changes embodied in the bills, which is to ensure an effective RET scheme overall – one that enables large-scale renewable technologies to be deployed and for the economy to capture the benefits of that deployment over time. The components of the bills that establish the Large-scale Renewable Energy Target (LRET) appear capable of serving this intention.

TRUenergy is however concerned about the components in the bills that establish the Small-scale Renewable Energy Scheme (SRES).

In TRUenergy's view, uncapped cross-subsidies, such the SRES, are most efficiently delivered directly to households from consolidated revenue sources, eliminating retail energy market pass-through concerns and the potential for distortions to energy market competition. If this is not possible, TRUenergy advocates using monopoly components of the energy sector to minimise pass-through concerns and potential distortions to competition. It is noted that the 'network alternative' was raised in the Government's discussion paper prior to the bills, but that it was not sufficiently developed in comparison to the other options analyzed in the consultation process.

Furthermore the practical approach adopted in the bills to give effect to this funding model imposes an unnecessarily convoluted and complex set of arrangements on all market participants (installers and liable parties). A large part of the problem arises because the SRES is uncapped in its volume and therefore liability.

Much of the convoluted and complex regulatory mechanics are only necessary to cap the SRES volume/liability each year while avoiding an overall scheme cap. It is understood

that this is an attempt to provide liable parties with a degree of certainty over their liability while maintaining a guaranteed subsidy level to suppliers of small renewable technology.

However, this approach fails to achieve either of these objectives, and does so at the expense of simplicity and administrative efficiency.

Problems with the current approach

1. Liable parties will be unable to fully hedge their exposure because they face an unknown obligation in quantity terms beyond one year (note, quantity uncertainty cannot be effectively hedged in this market):

- for adequate cost recovery in a competitive retail energy market, at least 2 to 3 years of cost certainty is practical and beneficial; and
- for regulated retail energy markets, 3 to 4 years of cost certainty would serve to maximize the chances of adequate cost recovery.

2. The subsidy offered to installers does not adjust with movements in market conditions (such as the exchange rate) and subsidy levels from other sources (jurisdictions' programs).

3. Small renewable energy technology suppliers are likely to be as interested in cash-flow as they are in the price they receive per SREC (both of which determine the subsidy value) and that under the optional clearing house approach, the price of an SREC may well be lower than $40 for that reason (and more 'frequent surrender' is a highly impractical and costly means of addressing this).

Retailers' hedging requirements

Effective hedging as currently practiced in the RET market requires a 2 step process:

- forecasting the RPP for the next 5 years based on capped demand; and
- purchasing RECs from the market when providing a fixed price to customers.

The approach embodied in the bills does not accommodate this.

The basics of TRUenergy's preferred approach

Features of a capped quantity approach:

- a target defined annually (until at least 2014) based on expected installations of PV and SHW;
- a penalty price (above $40/REC) to act as a scheme price cap (and to ensure compliance);
- incentives for forward contracting across surrender periods (to hedge exposure for liable parties and optimise cash flow for SREC creators/installers); and
- low compliance requirements and administrative costs as a result of using existing RET trading infrastructure (and participant compliance systems) and obviating the need for a central clearing house function.

Calculating a total SRET

A method for ensuring that small renewable energy suppliers/customers receive the subsidy they require under an SRES target would be to base the target on a projection of the historical demand for these technologies. To ensure the target is sufficient to subsidize any/all prescribed installations:

- annual forecasts of PV and SHW installation ought to include a margin for error that biases towards a higher rather than lower subscription (capped only by a penalty price cap at some premium to $40/REC);
- in terms of SHW, about 850k solar hot water units are installed Australia-wide and there are about 8m households (6.3m of which are free standing and therefore eligible for installation of solar hot water units); and
- the forecast ought to be physically capped by the stock of households (existing and new) in Australia.

Capping total scheme costs

A shortfall charge above $40/SREC could be applied to ensure that the target does not exceed expected policy costs. The penalty price level would be paid by liable parties if they failed to meet their obligations:

- this level ought to be above $40/REC but in line with the expected cost the Government is willing to impose on energy consumers generally (as a result of the SRES);
- the spot SREC price will trade at the marginal cost of creating SRECs (i.e. economic subsidy required to finance the underlying technology, all things considered); and
- if the target is sufficiently high then the spot price may settle around $40/REC (note, installers have an adequate subsidy no matter what the spot price is).

Enabling forward contracting across periods

Liable parties will be able to manage their SREC price risk under this approach in the same way they currently manage their REC exposure and LREC exposure post 2010. At present the existing market provides REC creators with an efficient avenue to monetise their RECs within a matter of days. This has proven a very effective way of assisting REC creators to fund their operations because of:

- the ability to bank SRECs for the duration of the scheme (i.e. inter surrender periods);
- the ability for retailers to forecast surrender requirement with a high level of accuracy; and
- the incentive for retailers to contract frequently with SREC creators/installers within the surrender period (driven by electricity pricing to customers).

Existing RET infrastructure allows for a responsive market

The price responsiveness/transparency of a market is of particular benefit to installers (receiving the subsidy) and energy customers (paying the subsidy) because it adjusts automatically to address the following situations:

- exchange rate fluctuations lowering the cost of technology to the point where installers are paying households to have systems installed; and
- jurisdiction subsidies are reduced to the point where some installers receive an insufficient subsidy for economic SREC creation.

Review

The entire SRES target could then be re-evaluated in 2014 (together with the LRET) and the case for its continuation, as well as the quantum of its targets, could be assessed.

Yours Sincerely,

[signed]

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