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Department of Environment, Land, Water and Planning
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By email: Renewable.Energy@delwp.vic.gov.au

Dear Sir/Madam,

Clean Energy Council submission to the Victorian Renewable Energy Auction Scheme Consultation Paper

The Clean Energy Council (CEC) is the peak body for the clean energy industry in Australia. We represent and work with hundreds of leading businesses operating in solar, wind, energy efficiency, hydro, bioenergy, energy storage, geothermal and marine along with more than 4,000 solar installers. We are committed to accelerating the transformation of Australia's energy system to one that is smarter and cleaner.

The CEC welcomes the opportunity to make a submission to the Victorian Renewable Energy Auction Scheme – Consultation Paper (the consultation paper). The CEC supports the development of the auction scheme as an important tool in creating jobs and investment, as well as driving change in the Victorian electricity sector. A well designed auction scheme will cement Victoria's leadership in the renewable energy industry as well as create clarity and certainty for investors.

The role of renewable energy in helping to reduce electricity prices and protect consumers state from rising fossil fuel prices is becoming more broadly appreciated among the general public. It is easy to understand why more than 80 per cent of Australians want to see more renewable energy.

This submissions follows the outline of, and answers the questions in the consultation paper.

Scheme structure

How can the Department ensure that a pipeline of projects will be ready to meet the Government's targets for 2020 and 2025 while maintaining appropriate flexibility for Government to adjust the scheme where required?

The most important action the Department can take to ensure that projects will be ready to meet the Government's targets is to proceed without delay. A staged approach will be useful to ensure that the government can proceed without delay, learn as we go and meanwhile undertake other strategies (outlined in this submission) to remove potential barriers to renewable energy investment.

We also recommend that the government focus on the design of the pre-2020 stage of the program. Details of the post-2020 phase can be considered at a later stage but the design of the pre-2020 phase needs to be decided upon as a matter of urgency.

We cannot stress too strongly the need for the Government to announce a clear decision on the way it will treat Large-scale Generation Certificates (LGCs) from the pre-2020 auctions and for it to stick with whatever decision it announces. This issue is addressed in greater detail later in this submission.

In order to improve the government's approach to planning approval CEC recommends the government consider establishing in Victoria the 'one-stop service' that the NSW Government makes available to developers in NSW. This approach would:

- Streamline and coordinate planning activities in the State.
- Harmonize Council fees. Every Council treats it differently and wants to have 'full cost recovery'.
- Coordinate airport issues under one agency

Victoria already has a significant pipeline of approved wind farm projects. However, many of these have old, out of date approvals that restrict technology to older models, making the projects less economically efficient. To ensure an adequate pipeline of wind farm projects the government should introduce changes to the planning scheme which allow for fast-tracked approval of project modifications.

Whilst the priority should be on enabling a fast start, and any reform of planning regulations should not hold up early investment, the Government should in parallel review the current planning framework in consultation with the industry to identify opportunities for improvement. To further encourage investment the Government should then put in place a more streamlined approach to new renewable energy projects

A key consideration for an efficient planning system is ensuring fast response times and enforceable processing timeframes for applications. Additionally, a fair and transparent system should allow developers and the community to know what is required to register an application. There is work to be done as soon as possible to clarify environmental impact guidelines, and the planning system should explicitly reference the environmental benefits of renewable energy projects.

In addition to good planning policy, developers will work toward the creation of a pipeline of projects only if they are confident that the auction scheme is not going to be abolished or substantially reduced in the near term.

A clear strategy that takes into account transmission capacity, demand profiles and therefore optimal project locations will allow more efficient concentration of effort into locations that will result in the most efficient state-wide energy system.

Finally, the Victorian Government can assist developers by ensuring transparency about the prices paid for projects in each auction tranche. This will allow developers who are working on projects to get a feel for if their projects will likely be 'in the running' or not.

How much notice should be provided to industry of upcoming auctions?

Approximately six months would be good, with anything over three months considered adequate. Firm commitment and public statements about the Government's longer term intent will be helpful for creating certainty in the market.

The Government should aim to announce winners as soon as possible following submission of bids, and try to time auctions so that they don't overlap with other processes.

Should capacity be auctioned in consistent capacity tranches (e.g. 200 MW etc)?

In order to run auctions at a reasonable frequency and get the required capacity built to meet the target the tranches will likely need to be larger than 200 MW. Consistency of tranche size isn't really important.

An important early consideration in deciding the size and frequency of auction tranches is defining the target. At the developer consultation on 23 August, the Government suggested that the target was to have enough renewable energy capacity actually generating throughout 2020 to make up 25 percent of generation. This means all capacity (an estimated 1,500 MW) will need to be operational by the end of 2019. This is a very ambitious target. Given that a large wind farm takes 24-36 months to actually construct, if the target were to be achieved primarily by wind farms then most of the 1,500 MW would need to be contracted in the first auction round in 2017. Large scale solar and smaller wind farms can be constructed faster than large wind farms, so would be able to deliver more quickly on the government's 2020 target. As a guide, a large-scale solar farm can be constructed in about 12 months. The government should consider running multiple auctions in 2017 and 'front loading' more than a third of the 1,500 MW in the 2017 auctions to increase the probability that the government's 2020 target can be met. We also recommend the government consider a large-scale solar 'carve out' for the first auction, scheduled for 2017. This will enable quick, visible delivery from the first auction and the experience of constructing large-scale solar in Victoria sooner rather than later will give the government more options for delivery by 2020.

The auctions should seek to select projects of various sizes. There is a place in Victorian communities for projects like Hepburn wind (4 MW) and Coonooer Bridge (20 MW), as well as smaller utility solar projects that can connect into more remote parts of the electricity grid.

At what frequency should auctions be held?

Approximately every six months should balance the administrative burden to applicants with the need to closely follow any potential price reductions and other efficiencies found in the market.

Depending on how progress is tracking towards the target, either the size of tranches or the frequency may need to be tweaked. As long as the Government is clear about this in advance it should not be a problem for developers.

What proportion of scheme generation should be dedicated to solar projects?

Large scale solar has enormous capacity for cost reductions, however the biggest enabler of these cost reductions is deployment of projects as this establishes supply chains, investment in staff training and experience in planning and network connection agencies. While Victoria does have a lower solar resource compared with some other parts of the country, it also has existing heavy

industry with potential transition opportunities for manufacturing to support solar engineering, procurement and construction.

A portion of at least 20 percent will ensure that Victoria can build the skills to ensure competitiveness in the large scale solar industry.

Should the proportion of solar be different pre and post 2020 to allow a solar pipeline to develop and technology costs to come down?

Costs of utility scale solar are coming down fast with or without the Victorian auction scheme. Large scale solar will roll out faster in sunnier states like Queensland and South Australia where the economics are more favourable, so Victoria is unlikely to be a cost curve driver. However, without deployment of projects in the state, these cost reductions will not be institutionalised in Victoria.

If the cost of solar drops below that of wind or any other renewable energy technology then it will be able to directly compete in the general technology neutral auctions. Victoria rightly notes that there are benefits in having diversity of generation types. A proportion of at least 20% should be maintained for large scale solar pre- and post-2020 to ensure that this is maintained. There would also be merit in having a higher proportion of solar in the earlier auctions to maximise the chances of quick results with projects generating well before the government's 2020 target date. Solar should not be restricted from competing in technology neutral auctions.

Are there any other matters the State should consider when setting the scheme's technology split?

The Government should be mindful of the cumulative impact of its program and limits on the extent to which it is possible (or beneficial) to co-locate multiple solar and wind farms. This would include limitations that might arise from grid capacity, for example. There may be some areas of the state that would be preferable for new projects to be located. It might be useful for the government to indicate it has preferred locations for new projects. However, ultimately it is the responsibility of proponents to manage the risks arising from where they choose to locate their projects.

What is the best way to treat LGCs under the scheme to enable successful proponents to secure project finance, ensure scheme costs are minimised and ensure adequate market interest from industry to participate in the auctions is attracted?

The most important thing that the Government could do to encourage financing of projects is to guarantee that the LGC component of any contract will be honoured regardless of what happens to the federal RET scheme. That is, even if the RET were repealed or the rules changed significantly, this should not affect the price that is paid by the Government under the auction scheme contract.

Treatment of LGCs and the structure of contracts are key considerations in the design of the Victorian Renewable Energy Auction Scheme (VREAS). It would be useful to undertake modelling to consider the effect that the auction scheme will have on LGC prices nationally. This could be undertaken in tandem with the auction process, and not as a precursor that might otherwise delay the commencement of the program. The federal Renewable Energy Target deadline is fast approaching and its achievement is in the national interest.

There are a number of principles or key objectives that could be set for the VREAS. The relative importance of the principles and key objectives will influence LGC treatment and contract structure. There are a range of views within industry regarding the most appropriate objectives and scheme design elements for the VREAS. To ensure balance and transparency this submission outlines the potential key principles and the design features that would best meet those principles. Ultimately it

is a matter for government to determine the principles that matter most to it. CEC would be happy to arrange further opportunities to discuss these issues in more detail.

1. Familiarity and track record

Some in the renewable energy industry have a preference for a system that is already familiar and that has proven successful. If the Victorian Government agrees this is an important principle then it should adopt, as far as possible, the approach that has been successfully pioneered by the ACT Government. This would involve conducting an auction for contracts-for-difference, in which renewable energy generators allocate LGCs to the government, with the expectation that government will extinguish the LGCs and not sell them to liable parties. The terms of the contracts require the government to pay the generator the difference between the agreed ‘strike price’ and the wholesale electricity price.

2. Minimising the role of government in the LGC market

There are some potential bidders who are strongly of the view that state governments should minimise their role in LGC markets. If this is considered an important principle it would logically lead to the conclusion that the government should auction a contract-for-difference, paying renewable energy generators the difference between the agreed ‘strike price’ and the sum of the wholesale electricity price and the LGC price. It would be the responsibility of the generator to sell its electricity and LGCs. This approach would minimise any uncertainty in the LGC market that would otherwise arise from the Victorian government holding a large volume of LGCs, which could potentially be either sold to liable entities or extinguished.

3. State governments as a ‘shock absorber’

The LGC market has been the subject of considerable uncertainty in recent years due to reviews and other interventions by the Federal government in the area of renewable energy policy. Some potential VREAS bidders have expressed support for the notion of the Victorian Government acting as a ‘shock absorber’, with the flexibility to sell LGCs at times when the market is highly illiquid or extinguishing LGCs if and when it becomes clear that the RET target will be met and further LGC sales would only serve to reduce prices. If it is considered desirable for the Victorian government to play an active role in the LGC market then, logically, the auction and contracts should be designed so that the government is the holder of the LGCs. This could be achieved using an approach similar to that adopted for the ACT Government auctions.

4. Minimising the cost of the Scheme to Victorian consumers

There are several views as to which approach would lead to the lowest Scheme costs. Some key considerations are summarised in the table below.

Design	Cost implications
CfD on electricity, proponent allocates LGCs to government and is responsible for selling electricity.	Will result in higher ‘strike price’ compared to a CfD on electricity and LGCs. Possibility of government recouping scheme costs if it sells LGCs. Uncertainty in LGC market could increase finance costs to developers beyond the VREAS. Very important for government to make clear its intentions regarding treatment of LGCs.
CfD on electricity and LGCs, with proponent	Will result in a lower ‘strike price’ compared to a CfD on electricity with LGCs allocated to government.

responsible for selling both.	<p>No opportunity to recoup costs through LGC sales.</p> <p>More risk on developer likely to mean higher finance costs.</p> <p>Difficulty with ensuring transparency around sale of LGCs and minimising costs to government.</p>
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What are stakeholders' thoughts about complementarity/additionality if the Federal RET were extended/expanded?

The Clean Energy Council supports the introduction of an ambitious federal scheme unifying emissions reduction goals and renewable energy goals by 2020. If this happens, the Victorian government should not legislate a separate, duplicate scheme but simply put in place further complementary measures like the 2020 goal.

In the case that by 2020 there is not a sufficiently ambitious federal scheme to meet emissions reduction commitments then there should be a separate Victorian scheme whereby LGCs are extinguished to ensure additionality.

The Government should be very clear about its intentions about LGCs after 2020. Project developers in other states, as well as in Victoria will be financing projects based on their views of future LGC prices and these projections are sensitive to what the Government does. If the Government signals that LGCs after 2020 will be extinguished, but decides instead to sell them on this could flood the market and have potentially dramatic outcomes for other projects.

Payment structure

Do stakeholders agree with the proposed CfD payment structure approach?

The Contract for Difference approach has been proven an effective and price-competitive scheme by the ACT Government, and it is the best approach for Victoria.

At the consultation on 23 August the Government suggested that it might give preference to projects with Power Purchase Agreements (PPAs) in place. This doesn't make any sense and will not assist those projects in getting built. The Government's scheme is the tool to get projects built and at a low cost of finance, and a PPA requirement should not be a consideration. Given that the margin on the PPA will be passed through to Victorian electricity customers anyway, there would be no economic advantage in requiring PPAs.

A contract-for-difference would play the same role as a PPA with regard to revenue certainty and the ability to obtain finance. The key difference between what the ACT Government offers and conventional PPAs is that the ACT government pays the difference between the spot price and the contract price, whilst the project still earns the spot revenue from AEMO. Under most retailer PPAs the retailer earns the spot revenue, keeps the LGCs and pays the project owner a fixed price per MWh each week or month. The key issue is longer term revenue certainty and without some form of contracting, finance is not available.

In fact favouring projects that secure PPAs will reduce the availability of PPAs for any projects that are under construction at the time of the first auction, taking a chance on the wholesale market with a view to securing a more favourable PPA in future.

Some potential bidders argue that the existence of a PPA should result in a project being disqualified from the VREAS program. The reasoning behind this is that if a project has a PPA it does not require a CfD from the government and the only affect will be that the PPA counterparty will be subsidized for something they are already required to do i.e. procure LGCs.

If a CfD payment structure is used, on what basis should a NEM reference price be set? (e.g. monthly average, half hourly NEM price)?

Half hourly prices will most accurately reflect the value of the electricity and will therefore have the clearest signal for building in locations with the best resources (that is, the best resources and at the most efficient times). Monthly averages will mask the correlation between demand and generation and lead to a less effective market.

It is unclear why the reference price should be a NEM average rather than just the Victorian reference price. The Government should consider using the Victorian reference price when calculating payments in the auction scheme.

What would be the impact of adding a floor price to cap the total payment applicable in any one period?

Adding a floor price will protect the Government from high payments when market prices go negative as a result of too much generation at times of low electricity demand. This will limit the liability of the Government and therefore minimise the cost which is eventually passed on to electricity users.

Setting a floor price removes the price certainty for generators (as in, they will no longer be guaranteed payment of the difference between wholesale + LGC and the strike price) during these periods and will introduce uncertainty into a scheme specifically designed to create certainty. This will result in a higher strike price.

There may be other mechanisms to avoid generators operating during negative price events, and those mechanisms should be explored. However, given that it is possible for generators to limit generation, a floor price is a fair and reasonable policy for protecting electricity users from unreasonable costs. It is important to note that setting a floor price will require half hourly reference prices.

Do stakeholders agree that payments should be made under the scheme based on energy delivered as defined above? Are there other ways that stakeholders consider are possible to provide locational signals to projects to ensure they are appropriately sited on the network?

The reference price should be calculated to include application of the Marginal Loss Factor (MLF) and Distribution Loss Factor (DLF). Using the price at the project meter will mean that loss factor risks are taken by the Government, whereas the risk should be borne by the generator. This will contribute to ensuring efficient geographical placement of generation assets. The Government should note that contracting of additional generators in the vicinity of existing generators may have an adverse impact on their MLF and/or DLF.

Do stakeholders consider that any alternative payment structures could be employed for the scheme, such as a fixed payment approach? If so, what are the relative advantages and disadvantages of these options?

The Contract for Difference approach will result in the lowest prices.

Do stakeholders agree that a fixed payment approach would be less likely to address the barriers faced by project proponents in relation to attaining project finance, resulting in lower value for money bids?

Revenue certainty is the main contributor to lower project costs and the contract for difference is the best approach.

Contracting elements

Are the above contract elements broadly appropriate?

The contracting counterparty should be the Victorian Government. Government is seen as the most dependable contracting party and this effects debt and equity margins. There is a real and significant cost saving to be found in maximising certainty and investor confidence at every opportunity.

A key requirement for developers to be able to obtain finance after winning an auction is a bankable contract (Deed etc) from the State that guarantees the project is entitled to being paid the revenue stream under the CfD scheme once it starts generating.

Banks/financiers will typically also require Tripartite arrangements to be in place at the outset, so that they can step in and take over should a problem with the project's ability to repay debt arise.

Within the contract range of 10 to 20 years, is there an ideal duration, particularly with the aim of minimising project financing costs?

Longer contracts result in lower prices because of reduced financing margins. A 20 year contract will secure very attractive pricing for the Victorian Government and minimise the cost that is eventually passed through to electricity users.

What would be an appropriate project delay threshold for contract termination clauses?

A reasonable period would be around 6 months to a year. This depends on the Government's definition of project commencement. This could be defined as reaching financial close/FID, giving notice to proceed to an EPC Contractor, or a down payment on turbines or panels. It should be kept in mind that larger projects will require longer timelines than smaller projects.

Would quarterly payments have a significant impact on financing costs compared to monthly payments?

Monthly payments would result in a slightly lower strike price which will benefit both the Government and electricity consumers.

What are the implications of a two-way CfD?

A two way contract for difference means that if the energy price is higher than the strike price then the project pays the Government. Project finance will be based on the strike price anyway so it is reasonable for the Government to get the benefit of any upside.

To ensure the two-way CfD is fair, the application of any floor price should be matched by a cap, or neither should be applied. On balance, a clean two-way CfD without a cap or floor is probably the simplest approach and this should not present problems for financing.

What do stakeholders think about the generation requirements being considered? Where maximum and minimum generation volumes are contained in scheme contracts how should these be set?

The Clean Energy Council does not support the generation requirements. Setting a maximum seems counterproductive to the achievement of the scheme. A better approach would be to monitor the generation from all projects and take this into account when measuring progress and making plans for future auction tranches.

A minimum generation target also seems counterproductive. Given that the Government pays per unit of electricity there is no risk to the Government for an underperforming project.

Are any of the elements likely to lead to perverse outcomes?

Given that the contracting period commences before the project is constructed, care should be taken to ensure that the strong incentive to start construction does not result in any corner-cutting or counter-productive time saving.

Scheme administration

What are the relative advantages and disadvantages of the different scheme administration and cost recovery options listed above?

Collecting the costs of the scheme through transmission charges would minimise administrative costs and result in costs being more equitably distributed across all Victorian electricity customers. For example, there are some large electricity users that are directly connected to the transmission network and avoid distribution network costs.

Collecting the costs of the scheme through distribution businesses would, in effect, exempt large electricity users directly connected to the transmission network. This could complicate the implementation of the government's stated intention to exempt electricity-intensive, trade-exposed companies.

Is there another mechanism for recovering scheme costs the Government should consider that would result in better outcomes?

CEC's preference is that the Government recover scheme costs using the existing framework of land taxes on transmission easements that currently funds the Smelter Reduction Levy. The Smelter Reduction Levy expires in 2016 and given that the structure already exists and has been proven legally sound, it should be possible to transition it to funding for the Victorian Renewable Energy Auction Scheme.

The Department's proposed position is currently to exempt emission intensive trade exposed companies (as defined under the Federal Government's RET scheme) from paying scheme costs. Do stakeholders agree with this approach? Are there any other parties Government should consider exempting from scheme costs? If so, how should this occur?

If trade exposed companies are to be exempted the exemption should only be extended to electricity-intensive trade exposed companies, rather than emissions-intensive trade exposed companies. Not all emissions-intensive companies are electricity-intensive. Electricity-intensive companies would be affected by the proposed cost recovery but emissions-intensive companies would not.

This issue of exemptions involves both political considerations and practical matters of implementation. The political issue relates to allocation of costs. Exempting electricity-intensive trade exposed companies from paying scheme costs will result in higher costs being borne by customers that do not meet the eligibility criteria for exemption.

There would be significant barriers to implementation of proposed exemptions for electricity intensive, trade exposed companies if costs are recovered through either distribution or transmission network charges. Network companies simply do not have access to the information needed to properly identify eligible customers. Providing exemptions to network charges could run afoul of the National Electricity Rules. It is unclear whether network businesses are permitted to set new tariff classes for electricity intensive, trade exposed customers. It would be preferable to manage an exemption framework outside of network charges (eg. with direct payments from government to the exempt companies).

Evaluation criteria

What do stakeholders think of the proposed evaluation criteria set out above?

The evaluation criteria are mostly good, and value for money, economic development and community engagement are all very important. The Government should be very clear about desirable economic benefits and should require the demonstration of tangible benefits.

Prioritising timely construction will likely favour solar projects over wind and smaller projects over larger. Larger projects are often able to commission sections as construction continues so this evaluation criteria may not be very useful.

The criteria about contribution towards the target is strange. While the auction tranches will be in MW capacity bundles, the Government will only measure and pay for electricity delivered. Therefore there's no reason to favour a project with a higher capacity factor, as a more efficient project should naturally come up with a lower cost of energy

Do stakeholders have views on how evaluation criteria might be weighted?

The highest weighting should be given to value for money, with a secondary weighting for economic development. However, it should also be noted that the more requirements there are regarding economic development (eg. local job creation or local manufacturing content), the more restrictive this will be on developers in terms of optimising their projects and this could lead to higher costs. Community engagement is important and Government should look for projects that can demonstrate effective engagement, remembering that sometimes it is not possible to avoid criticism from vocal anti-development lobbying groups.

Are there other evaluation criteria/principles that the Government should consider to ensure the scheme meets its objectives?

There is an opportunity for the auction scheme to include other Government priorities in addition to jobs, investment, and emissions reduction. For example, the ACT Government's scheme included a requirement for educational outcomes, and winning projects undertook initiatives including setting up university courses and visiting high school students. The Victorian Government may want to tie the auction scheme to its separate STEM education projects, energy efficiency targets, environmental projects like native vegetation protection or planting, or other outcomes.

