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Department of Environment, Land, Water and Planning  
PO Box 500  
Melbourne VIC 8002

By email: [renewable.energy@delwp.vic.gov.au](mailto:renewable.energy@delwp.vic.gov.au)

Dear Sir/Madam

## **NAB SUBMISSION TO THE VICTORIAN RENEWABLE ENERGY AUCTION SCHEME CONSULTATION PAPER**

The National Australia Bank (NAB) welcomes the opportunity to contribute towards the Victorian Renewable Energy Auction Scheme consultation process.

NAB believes that a well-designed auction scheme will assist the Victorian Government to achieve its targets whilst creating jobs and attracting investment to the State. In designing the scheme, we recommend that the Government keeps certainty in regulatory matters and the pipeline of opportunities at front of mind. A simple framework with well-defined risk allocation also needs to be adopted to attract the most efficient outcome for the State – and importantly – the end Customer.

This submission (Appendix 1) follows the outline of the consultation paper. We have chosen to respond to those questions which are particularly relevant from a financier's perspective.

### **ABOUT NAB**

As the leading arranger of project finance to the renewable energy sector for the past ten years, NAB has extensive experience in structuring, financing and advising on renewable energy project requirements including the ACT reverse auction schemes. Since December 2014, we have accelerated and broadened our environmental financing activity, including a number of industry-leading initiatives such as launching the first Australian bank-issued Climate Bond Standards certified Climate Bond, arranging the first renewable transaction to feature in the US Private Placement market, entering into a partnership with the City of Melbourne to source renewable energy via a group purchasing model and role as Sole Arranger for the launch of the Victorian Government Green Bonds.

NAB is committed to continuing to support the clean energy sector and developing models to increase uptake of renewable energy. Demonstrating this, in November 2015 an organisational commitment was made to undertake financing activities of A\$18b over seven years (to September 2022). In 2016, NAB also became the first Australian bank to become a corporate member of the Clean Energy Council, Australia's peak body for the clean energy sector.

This long-standing commitment to action on climate change is reflected within our business. NAB was the first Australian bank to achieve National Carbon Offset Standard carbon neutral certification in 2010. More recently, we committed to source 10% of NAB's Australian electricity from new and additional renewable energy projects by 2018 – to stimulate growth in the renewable energy sector. NAB's participation in the Melbourne Renewable Energy Project and direct investment in renewable energy generation at our facilities are considered central pillars to the realisation of this goal.

NAB has also set a science-based greenhouse gas emission reduction for our operations; supporting the internationally agreed objective of limiting global warming to less than two degrees Celsius above pre-industrial levels.

As a Melbourne headquartered company and one of Victoria's largest employers, NAB is pleased to be the first major bank to sign up to the Victorian Government's Take2 Pledge and support the State-wide 2020-2025 emissions target.

If you would like to discuss NAB's submission in further detail, please contact

Regards

A handwritten signature in black ink, appearing to read 'Steve Lambert', written over a light blue horizontal line.

**Steve Lambert**  
Executive General Manager, Capital Financing  
National Australia Bank

## Appendix 1

### 1. 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?**

In order to meet the Government's targets by 2020 and 2025, the Department will need to ensure that the scheme is brought to market as soon as possible. It is important that a well-planned timetable for the scheme is devised with key milestones established for the submission, evaluation and determination of successful projects from the outset, to assist proponents to properly prepare for the auction process.

We recommend that the Department ensures simplicity in the scheme design and appropriate risk allocation between the various stakeholders to ensure the most efficient debt and equity proposals are achieved. Certainty in respect of the scheme design will provide confidence to proponents and will assist in securing non-recourse financing in respect of potential projects.

The successful implementation of the scheme will also require a streamlined approach to other aspects of project delivery (such as planning and network connections). NAB recommends that the Government works with other stakeholders to ensure that projects can be efficiently delivered at the most competitive price.

The creation of a pipeline of opportunities, through clear visibility of the proposed tenders, will ensure greater investment interest and assist in achieving the Government's proposed targets for 2020 and beyond.

Collaboration with Regional Development Victoria, and other relevant government Departments and agencies, would also be valuable to help identify and promote development of renewable energy assets in areas of the State best suited to these projects. This collaboration should also be directed towards streamlining and assisting the development approval process, as well as to assisting with regional stakeholder engagement in order to build support for development of renewable energy generation assets across the state. Where other Departments have relevant assistance funding that project proponents could apply for to help get their projects investment ready, this support should be communicated early to help build the project pipeline as quickly as possible.

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

Based on our extensive experience in advising and arranging financing for renewable projects, we recommend that at least six months notice be provided for each upcoming auction to ensure that project proponents can appropriately prepare submissions for projects, including debt proposals. Following each auction, it is critical a decision is made efficiently, and this period is kept to a minimum, to reduce foreign exchange and interest rate movements from the bid date to the selection of the proponent.

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

As noted above, visibility of the project pipeline is the most critical issue for industry – consistency in capacity tranches is less relevant. We recommend a minimum level of 200MW per tranche to ensure competitive tension and assist in meeting the 5,400MW target in a timely fashion.

**At what frequency should auctions be held?**

We recommend that auctions be held approximately every six months to allow sufficient time between processes for proponents to prepare submissions.

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

NAB is the leading provider of renewable energy financing and is demonstrated by our track record in providing finance for on and offshore wind, solar, waste to energy and other renewable energy projects. We support and will continue to support wind, solar and other clean energy projects. Based on our experience, we believe there will be sufficient liquidity to support the development of wind and solar projects in Victoria.

**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?**

In designing the auction scheme, the Government needs to be conscious of the impact it may have on existing renewable energy projects and stakeholders. The design of the scheme should ensure to the best extent possible that the ability of existing projects to re-contract in the future is not negatively impacted, as this would have a detrimental impact on investor confidence. Similarly, any scheme should aim to minimise any potential market distortion, whilst still continuing to encourage new investment in clean energy.

**What are stakeholders thoughts about complementarity/additionality if the Federal RET were extended/expanded?**

We recommend that the Victorian Government coordinate with the Federal Government to ensure that additionality and complementarity requirements are appropriately maintained and managed. Additionality is an important principle that underpins the credibility of Australia and Victoria's performance against greenhouse gas mitigation targets. It also underpins consumer confidence in buying and paying a premium for renewable energy.

It is in the best interests of existing stakeholders to ensure there are no unintended consequences of the scheme for investors who have made investment decisions based on 20 year plus investment horizons.

## **2. Payment Structure**

**Do stakeholders agree with the proposed CfD payment structure approach?**

Contract for Difference (CfD) has been bankable in the past in other jurisdictions such as the ACT and QLD (Solar 120). NAB will continue to support projects with CfDs subject to the stability of cash flows. The matter of cash flow stability is expanded further in our response to the next question.

**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)?**

The NEM reference price should be consistent with the existing AEMO settlement method and aim to eliminate basis risk. Basis risk is the difference between the NEM Reference Price in the CfD contract and the underlying electricity price received by the project. Any basis risk reduces the bankability of the project.

AEMO currently settles on a half hourly basis, and using this as the NEM reference price in the CfD contract will reflect the settlement price which would have been received by the project (before adjustments for MLF & DLF) if it was generating as a merchant operator.

**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 sighted on the network?**

It is important not to create additional mechanisms or incentives that could influence the location of projects. The existing MLF and DLF mechanisms AEMO has in place create discipline on projects and ensure investments are located in suitable locations. The Victorian Government should rely on these existing mechanisms which already exist in the currently competitive market.

**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?**

Yes, NAB agrees. A CfD provides greater revenue certainty to project proponents whilst incentivising for suitable project design and location. This is expected to result in lower bid prices.

### **3. Contracting Elements**

#### **Are the above contract elements broadly appropriate?**

The Victorian Government is in a position to leverage its strong credit profile to minimise overall financing cost. NAB considers that overall financing costs would be minimised if the direct counterparty is the State itself, rather than a department or sub-sovereign institutional entity. Based on our experience as the leading national financier of Infrastructure investment and long history of PPPs, this issue has been comprehensively considered with governments and market competitive forces have determined that direct State contractual counterparties deliver superior outcomes in terms of cost of capital.

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

Longer dated contracts allow capital servicing to occur over a longer horizon. This directly reduces overall financing costs and thus lowers the required contract price and minimise the cost to government. NAB therefore considers that 15-20 years is an ideal contract duration.

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

Market precedent has shown that the market will accept delay thresholds for termination or sunset dates with a minimum of 12 months after the expected commercial operating date. Shorter sunset periods will increase risk to project financiers and result in higher costs. Delay and termination clauses will also require appropriate extensions or adjustments for force majeure events.

#### **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?**

Minimum generation clauses increase the risk to project financiers, noting that the impact depends on the proposed severity of the consequences of failure to meet. Financiers will require suitable mechanisms to be included in contracts as a first pathway to cure any failure to meet a minimum generation condition prior to contract termination. Precedent based on previous successful financing suggests that minimum generation clauses be set at an independently verified (via technical due diligence) 1-year P(99) production threshold. Minimum generation tests and clauses will also require appropriate adjustments or exemptions for force majeure events, with the specific requirements being subject to the proposed severity of the consequences of failure to meet.

NAB has no position or view on maximum generation volume limits or clauses.

#### **Are there any other contract elements that should be considered?**

The contracted cash flows are potentially exposed to both future Federal and Victoria Government renewable energy policy changes, hence our earlier comments on the desire for policy consistency over time. Any termination clauses due to change in state or federal policy will require compensation adjustments.

Standard tripartite agreements between the project, State and financiers will be required to facilitate non-recourse finance.

#### **4. Auction Evaluation Principles**

**Would there be benefit in asking proponents to submit expressions of interest to participate in the auctions to ensure only more advanced projects proceed to the full evaluation round and that costs are minimised for project proponents where possible?**

Evaluation criterion should include an assessment of the proposed projects' financing plan. High merit projects should include a credible financing plan, which also provide evidence for support that the project can actually be financed at the proposed bid price. Projects presenting a credible financing plan achieve multiple aspects of execution de-risking for the government including:

- a) the project's commercial and technical plan is likely to be more advanced, and will have passed at least a preliminary due diligence/ sense check by financiers;
- b) the project will be more likely to successfully achieve financial close if selected as a winning bidder; and
- c) the project is likely to achieve financial close (and thus start construction and production) faster after being selected as a winning bidder.

## **Appendix 2**

### **NAB's Climate Change Commitments**

In the lead up to the Paris Climate Conference in 2015, NAB established a new climate change statement and five new climate change commitments, as follows:

#### **Statement**

NAB Group recognises that climate change is a significant and complex challenge requiring action at all levels of government and by all stakeholders.

NAB believes an effective United Nations agreement will provide both context and a framework for national actions and policies, facilitate international cooperation, and address the challenge of climate change. This includes supporting the globally agreed goal to limit global warming to less than 2°C above pre-industrial levels, as well as giving regard to science-based reduction targets and the policy and market mechanisms necessary to assist in achieving greenhouse gas (GHG) reductions. An effective international agreement should assist in providing business with the certainty and frameworks it needs to scale up global investment in low carbon technologies and infrastructure and lead to the creation of significant new business opportunities.

NAB believes the financial sector has an important role to play in assisting the transition to a low carbon economy, through both the energy we purchase directly and through financing. This transition however, needs to take place in a considered and balanced manner, supported by a stable policy environment that can underpin the transition and provide investment certainty over time.

#### **Our Five Commitments**

In recognition of the role NAB can play in supporting the transition to a low carbon economy that limits global warming to less than 2°C, NAB has adopted three "We Mean Business" Coalition climate change commitments. In addition, we make two further commitments that demonstrate NAB's intention to continue to take a leadership role through how we source energy for our operations and support our customers through financing activities.

1. Undertake financing activities of A\$18bn over the seven years to September 2022 to help address climate change and support the transition to a low carbon economy
2. Source 10% of NAB's Australian electricity demand from new and additional renewable energy projects by 2018
3. Engage responsibly on climate policy
4. Report climate change information through mainstream reporting channels
5. Commit to putting a price on carbon and align to the UN Global Compact's business leadership criteria on carbon pricing

Further information on our environmental commitments and activities can be found at [www.nab.com.au/environment](http://www.nab.com.au/environment).