Landfill Gas & Power Pty Ltd
Use Your Power to Make a Difference

Submissions
Climate Change Authority
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RET Submission – Landfill Gas & Power Pty Ltd

Dear Sir/Madam

Landfill Gas & Power Pty Ltd thanks the Authority for the opportunity to make the following submission in relation to the Renewable Energy Target Review.

Background

Landfill Gas & Power Pty Ltd (LGP) has been in operation since 1993 and has established itself as a boutique producer and retailer of renewable electricity in Western Australia. LGP's retail operations pre-date the deregulation of the electricity market in Western Australia through special agreements and LGP was one of the first movers when deregulation commenced in the late 1990s. LGP is also a market leader in the development and management of efficient waste-to-energy technologies in Western Australia. Its core business is extracting methane, one of the more harmful of the greenhouse gasses (GHG), from landfill sites and converting it into a safe, clean and reliable renewable energy source.

Currently, LGP manages the gas emissions from six landfill sites within the Perth metropolitan area and built, owns and operates three waste-to-energy power stations which are located adjacent to these landfill sites. A further two power stations have been closed due to fuel depletion, with one having been converted to diesel operation. LGP generates approximately 75GWh (75,000,000kWh) of renewable electricity per annum which is sold to around one hundred private customers operating over 370 sites connected to the South West Integrated System (SWIS) in Western Australia. Most of these customers are medium size enterprises, such as small industrial operations, hotels, supermarkets, shopping centres and schools. Of particular note, LGP is a Preferred Electricity Supplier of the WA Local Government Association (WALGA). We also supply large industrial enterprises such as WesTrac and the Southern Metropolitan Regional Council's Waste Management Facility at Canning Vale.

Current RET Effects

LGP is thus both a generator of renewable energy, which entitles it to create Large Generation Certificates (LGC) above a regulatory baseline, and a retailer of energy, whereby it bears primary liability for RET imposts in relation to its "*Wholesale Acquisitions*" of energy for its retail customers.

LGP pays royalties to the Regional Councils for the use of landfill gas, thereby generating a revenue stream for these Councils to the ultimate benefit of their ratepayers. These royalties are based on the revenue from selling LGCs as well as from electricity generation operations. In capturing and utilising the methane that would otherwise be emitted by landfills, LGP's activities also reduce the Carbon Price liability of those Councils at no cost to those entities.

Effect of RET Changes

Large changes to RET policy are likely to damage not only the LGP business from the loss or reduction of revenue but also have major negative impact on Councils both from the loss of revenue streams from LGC and electricity royalties and, in the worst case, where generation from LFG sources becomes unviable, significant potential increases in Carbon Price costs. Such outcomes will of course have direct impacts on ratepayers and businesses through increased rates and charges to cover lost revenue and/or increased costs.

LGP supports the current RET model in most cases although there is potential to increase the possible scope of the RET beyond 2020. Changes to the RET to create a floating percentage of demand, rather than a fixed amount, and to base this on demand projections, carries issues as to the viability of the potential for landfill gas projects to operate in the long term. Furthermore, with the recent changes to split the scheme between large and small scale generation, LGP is supportive of the current market structure and operation of the RET overall but sees the longer term desirability for including a cap on the STC scheme.

The single largest issue with potential changes to the RET is that these changes will have a long term disincentive for businesses to enter into or continue long term investment in the renewable energy sector. Uncertainty and instability which has been problematic for the industry over recent years needs to be removed and longer term policy stability needs to be maintained. Furthermore, programs and policy once agreed and set should not be changed at the last minute (e.g. removal of grandfathered landfill gas sites from inclusion in the CFI) which damages business confidence in both the short and long term. The renewable energy industry needs sustainability not only for their own businesses, but also for those of key stakeholders who will be impacted by poorly considered changes.

LGP Position on the LGC questions posed

- ***Increasing the RET after 2020***

An increase in the RET after 2020 is desirable based on the assumption that there is still an economic rationale for the continuation of support for increasing renewable energy generation beyond the current 41,000 GWh target. While there is currently ongoing investment in new renewable energy capacity, fossil fuel emitting technologies are unlikely to be significantly reduced over the period from now until 2020 even with a Carbon Price. In many cases there is significant investment in additional fossil fuel generation capacity, primarily though coal seam methane and other methane based sources. Unlike landfill gas operations, which are aimed at reducing overall GHG emissions, this additional generation capacity will continue to increase Australia's carbon emissions total.

In addition to the current situation of increased fossil fuel capacity, fossil fuel based technologies are currently receiving both implicit and explicit subsidies from both state and Federal Governments that support their continued operations; renewable energy generation does not receive the same level of subsidy and support. Examples of these subsidies include:

- pricing subsidies for coal generation in some states;
- direct grants and subsidies to coal producers improve thermal efficiency or reduce greenhouse gas emissions;
- $0.23 / kWh depreciation charges for coal fired generation;
- accelerated write offs for fossil fuel exploration; and
- fuel tax credits for mining (coal price subsidy).

As these subsidies are directed to s fuel supply chain they are 'hidden' from the electricity market, unlike the RET which is directly seen in wholesale and retail electricity market pricing. It is unlikely that these subsidies will be significantly addressed prior to 2020 and as such, as a mechanism of market equity the RET as a support mechanism needs to be continued.

Other than the RET, there are no subsidies for renewable energy. The RET is a market-based price while fossil fuel support is 'hidden' in the form of forgone tax revenues and upstream cost support. The Carbon Price has been argued as making the RET redundant and that not only should it not be increased past 2020 but it should be removed altogether. This would be a significant blow to Australia meeting long term renewable energy generation targets.

The proponents of the removal of the RET state a Carbon Price alone will be sufficient to support the development of additional renewable energy capacity past 2020. However, the Garnaut Report identified that a carbon price of at least AU$40 would be needed to ensure that level of renewable energy adoption in the absence of the RET[1]. Recent changes in the Carbon Price legislation to align the Australian Carbon Price with the European scheme and the removal of the Australian price floor creates a risk that a price of $40 is unachievable in the long term. Such a risk undermines the argument that the RET should be removed or reduced.

Without both a Carbon Price and the RET it is feasible that Australia will be unable to meet its 2020 renewable energy target. The key issue with the retention of the RET is that it does not only act to reduce emissions intensity in the stationary energy sector but it also assists in the longer term through the building of industry capacity to reduce the cost of adoption for renewable energy[2].

In addition to the issue of the Carbon Price and its market value, the Carbon Price itself is still the subject of significant political uncertainty. The current Coalition policy is for the removal of the Carbon Price (should it win an election in 2013). This means that significant changes to the RET in light of Carbon Price at this time would create risks for renewable energy generation businesses should the RET be reduced and the carbon price then repealed. These risks would be focused around the long term reduction in value of LGCs and compromising the current value of investments. In doing so this would undermine business confidence in investment in future renewable energy generation.

Without continued support for the RET after 2020 and the opportunity to increase the scale of the RET beyond 2020 to encourage increased investment, there is also significant risk that Australia will not reach its committed long term renewable energy targets.

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[1] Garnaut, R (2008) The Garnaut Climate Change Review

[2] Philbert, C (2011) Interactions of Policies for Renewable Energy and Climate, IEA

- ***The RET as a fixed GWh generation target***

LGP supports the proposition that the RET should be a fixed generation target denoted in GWh rather than a percentage target of projected future electricity demand; the percentage of renewable energy then becomes a function of a fixed GWh target for generation based on the total electricity demand in a year.

Basing the RET obligations on an estimate of the percentage of demand for a year creates uncertainty as to the scale of future RET obligations. Without certainty on the target, the increased risk exposure and uncertainty factors must be priced into bilateral contracts for energy supply. A 'floating' renewable energy target creates a greater uncertainty for businesses who have RET Wholesale Obligations to acquit; particularly in cases where these businesses have multi-year bilateral contracts which often have limited scope for accommodating changes of this nature – the practice of pass-through of such changes to end-users merely shifts the balance of risk and cost and restricts the potential for Retailers to provide least cost electricity supply alternatives. The pricing risk for small retailers acts as a significant disincentive for these businesses as they:

- are less able to absorb this price risk compared to large retail entities and
- are less able to pass on the price risk within a contract without becoming uncompetitive in the marketplace; and
- are often unable to pass on additional costs directly due to pricing being tied to regulated tariffs.

Small to medium retailers cannot afford not to account for this uncertainty as it is a cost that is not necessarily easy for them to absorb. Considering the recent examples demonstrating that estimates and projections of future energy demand and consumption are often highly inaccurate and difficult to predict (AEMO etc.), the use of a percentage of demand estimates rather than a fixed amount is problematic.

- ***Annual changes to the RET amount for large scale generation***

As discussed above, energy forecasting has recently been shown to be problematic, with a rapidly changing Australian economy and changes in energy consumption behavior that were poorly foreseen by market operators and many within the industry, particularly in the creation of network capacity. LGP sees that creating a circumstance where there is constant revision of the RET based on annually changing projections has long term negative impacts on businesses both in the generation and retail sectors, becoming more apparent as the 2020 deadline approaches. These negative impacts come from:

- Uncertainty as to the supply and demand pricing of LGCs in the long term, seeing investments in renewable energy generation infrastructure being considered increasingly risky or unworkable by the finance community, and Retailers increasing risk margins within electricity supply contracts;
- Increasing the uncertainty about overall government policy positions and the consequent sovereign policy risk. This has been an issue for the renewable energy industry over the past five years e.g. such policy changes seen with Solar Homes & Communities, REC multipliers, Feed-in-Tariffs, failed ETS introduction in 2009 and the 2010 RET structural changes;
- The impact on long term investment decisions which may be highly sensitive to a more volatile LGC market over the life of the investment due to changing annual obligations; and

- The accuracy of forecasts fails to allow for the appropriate risk pricing in long term contractual obligations for electricity supply which must include RET obligations.

The long term nature of investment into energy generation and bilateral contracts of supply means that rapid revisions of targets can actively discourage rather than encourage renewable energy investment, the exact opposite of the stated purpose of the RET.

Just as a fossil fuel generator needs to secure long term fuel supply contracts to maintain control on its long term sustainability, projects relying on the operation of the RET to secure their financial viability have a similar need for the stability of the scheme to ensure they are able to maintain sufficient revenues to continue operating with profit.

Furthermore, making the RET a 'moving target' is problematic for both generators and retailers as it creates additional compliance costs to energy pricing, creating a more complex and difficult environment for smaller energy suppliers in the market. Increased costs of business and operation act as a barrier to entry to, or remaining in, the market. This has the potential long term effect of lessening of overall market competition. That is to say smaller scale businesses are placed at a disadvantage when compared to their larger, more dominant competition as they are less able to absorb these additional costs.

Any change revision should not reduce the RET target below the existing 41,000 GWh target. It must be remembered that the policy intent for the RET has always been for **"at least 20 percent"** renewable energy, not **"no more than 20 per cent"**. Encouraging additional replacement of non-renewable sources with renewable energy increases Australia's long term energy security and reduces reliance on finite energy sources.

- ***Changes to pre-existing renewable energy generation.***

Changes in pre- existing RE generation capacity are unlikely to have a significant impact prior to 2020, other than reducing ability for hydro to contribute due to weather effects such as drought. Smaller renewable energy generation capacity may also need replacing in that time e.g. depletion of landfill gas resources and the like but this is unlikely to have an overall material impact on the achievement of longer term renewable energy targets.

The majority of new renewable energy investments over the past few years and into the foreseeable future are likely to have operational lifespans well beyond the current scope of the RET and will not be retired in this period. As such they become a fixed part of the RET.

- ***Appropriateness of the RPP methodology and the timing of the compliance year***

The current method for determining the individual entity obligations under the RET is the most reasonable and appropriate method for currently dealing with RET obligations. There have been no viable alternative suggestions on how the RPP methodology may be varied and it is difficult to see if there are any other alternatives which would not disadvantage smaller retailers.

- ***Is it appropriate to set the RPP by 31 March of the compliance year?***

The setting of the RPP by March 31 of the compliance year is seen as highly problematic as it stands since it does not allow for any flexibility or planning by businesses. While non-binding percentages are issued by the regulator up to two years in advance based on modeling

predictions, these are often insufficient for long-term planning. In the case of STCs and the STP (see below) it can have a large impact on retailers, particularly those who rely on bilateral contracts. Such a model increases compliance costs for energy retailers but currently no better models have been proposed and retailers must price in the risk inherent in the current market structure.

LGP Position on the STC questions posed

- ***Costs and benefits for the small-scale technologies scheme?***

From the position of both a retailer and generator, LGP agrees with the separation of the small scale and large scale technologies schemes with the RET. This is primarily due to the dilution of the value of LGCs by a large influx of 'phantom' RECS from the Solar Credit multiplier. While additional administrative and compliance costs are incurred by a small scale scheme, these are outweighed by the maintenance of the integrity and market pricing for LGCs. While there remains an 'overhang' of RECs/ LGCs from prior to the separation of the scheme, this is primarily a short-term problem.

As both a generator and retailer, LGP appreciates there are fewer problems with an integrated scheme if a business is just a retailer or their main generation assets are non-renewable. However, where a business relies on renewable energy generation and the price support from RECs to assist in maintaining a sustainable business, the dilution of RECS is an issue in long term viability. In the case of LGP and similar businesses, there is also an external effect in reducing the value of LGCs in reducing royalty revenue to landfill owners, such as local government authorities, who would then have to increase rates and taxes to make up for this revenue reduction.

- ***Maintaining large and small scale technology separation***

The structural separation of the small and large scale programs is relatively new and a response to a significant policy issue that developed from the Solar Credits Scheme. It is LGP's view that this separation is in the long term best interest of both small and large scale generation sectors in maintaining the integrity of the RET in encouraging renewable energy investment.

Now that the structural separation of the schemes is in place, the different market price signals for each sector can act independently to increase both small scale distributed generation as well as investment into large scale generation plants. Re-integration of the two schemes would likely again cause confusion in market price signals and devalue LGCs. This would again damage existing businesses and undermine confidence in long term policy stability, a necessary component for future investment.

- ***Is the uncapped nature of the SRES appropriate?***

While it is unlikely that there will be another 'boom' in small scale technologies as seen in the uptake of Solar PV by households, which was a caused y a combination of overly-generous feed-in Tariffs and the Solar Credit multiplier, the uncapped nature of the SRES makes this a possibility. In not having a cap, it effectively increases the potential for increasing additional liabilities for energy retailers under their STP obligations.

With the SRES remaining uncapped, additional risk is transferred to retailers for increasing obligations. Again, this cannot always be passed on to customers under bilateral contracts, so there is a disincentive for smaller retail electricity businesses that do not have additional resources to absorb uncapped costs.

The need to cap the SRES creates greater business certainty for obligated parties, the current uncapped nature making potential significant liabilities in future possible. An example of this has been seen in the current RET year where the obligations under the Small Technology Percentage (STP)reached 24% compared to the expectations of between 14-18%, creating again a problem with increasing unrecoverable costs for retailers.

Based on current trends, it is unlikely that the implicit target of 4,000 GWh for the SRES will be reached by 2020 without a significant further decrease in the cost of small sale systems in terms of their levelised cost of energy (LCOE) and continued large increases in the cost of retail energy for small scale residential and business consumers. Without these changes, there is unlikely to be large scale uptake of small scale systems as seen in the 'boom' periods in 2010-11 with the combinations of FiTs and the Solar Credits multiplier.

However, even with the SRES potentially falling short of the target, there is no specific reason for the scheme to remain uncapped. Future opportunities to adjust any capped systems remain and there is no reason at this time why the system should remain uncapped and create additional uncertainty and risk for electricity retail businesses.

- ***The role of multipliers in the RET***

It is LGP's view that there is no role for multipliers within the RET and there are better and more efficient mechanisms for the support of renewable energy generation. The inclusion of a multiplier for the RECs at the time had a significant impact on the value of Certificates and increased the obligations for the market to pay for this increase without a concomitant increase in the level of generation actually occurring. The creation of the 'phantom' RECs by the multiplier for Solar Credits had a negative set of impacts including:

  - Dilution of value for RECs at the time, acting as a disincentive for businesses to make additional renewable energy investment; and
  - Increasing the liability for businesses who are obligated to pay for these RECs and those costs being wither absorbed by those businesses or adding costs to retail energy users.

The multiplier effect shifts the cost of policy implementation from the Government on to the market, effectively cannibalizing the value of Renewable Energy investment. Furthermore, the experience for energy retailers who effectively pay for this has almost been entirely negative in relation to the uncertainty that the multipliers have created and the additional cost.

Based on this experience, LGP does not see that there is sufficient reason to introduce a multiplier for STCs in the future without again causing large scale distortions of the market and unnecessary additional costs for retailers and consumers.

- ***The STC Clearing House issues***

It is LGP's view that the STC Clearing House is operating as intended and there are no changes required to its operation. The Clearing House operates as a safe harbour for both investors and obligated parties. Investors can remove their STCs from the Clearing House at

any time that they need to and sell these on the open market. It also operates as an automatic hedge for retailers and obligated parties, ensuring that they are able to have a price cap of $40 and are not subject to excessive pricing for purchasing STC above this value.

The potential change to the operation of the Clearing House that has been suggested by some small scale system retailers is including a requirement for energy retailers to buy a certain percentage of their STC obligations from the Clearing House as part of their STP. Following this path, the requirement to buy from the Clearing House would add additional imposts to the retail cost of energy at a higher than market price. Effectively, a compulsory purchase percentage would be a de-facto tax on profits, as it would not necessarily be recoverable from consumers and it would have little benefit for either energy retailers or consumers.

In addition to the lack of overall benefit for the market, requiring a percentage purchase from the Clearing House would be economically inefficient as the market price for STCs are well below the Clearing House Price of $40. As noted, as investors or holders of RECs have the opportunity to sell at any time on the open market, those who are most efficient in their buying and selling practices reap the greatest benefit without adding upwards pressure on energy pricing.

- ***STC clearing house prices***

LGP supports the current pricing for STCs within the clearing House at $40. As noted above, the Clearing House price acts as both a safe haven for STC owners as well a hedge against shortages for retailers. The Clearing House price is effectively a cap in that there is no point in a business purchasing STCs on market at a price higher than the Clearing House price. As the current market is functioning adequately and the price has never exceeded the Clearing House price, there is no need to change the current price structure.

Should there be any aspects of the submission that require amplification or discussion please do not hesitate to contact the undersigned.

Yours Faithfully

Anthony Leahy
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