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Clean Energy Finance Corporation Expert Review Panel

Lodged by email: cefc@treasury.gov.au

Clean Energy Finance Corporation Expert Review

The Energy Supply Association of Australia (esaa) welcomes the opportunity to make a submission to the Clean Energy Finance Corporation (CEFC) Expert Review Panel on the design of the CEFC.

esaa is the peak industry body for the stationary energy sector in Australia and represents the policy positions of the Chief Executives of over 40 electricity and downstream natural gas businesses. These businesses own and operate some $120 billion in assets, employ over 61,000 people and contribute $19.3 billion directly to the nation's Gross Domestic Product.

Summary

esaa has previously commented on the CEFC in submissions to the Government on the Clean Energy Future Scheme exposure draft legislation and to the Joint Select Committee on Australia's Clean Energy Future Legislation. In these submissions, esaa argued that while there could be a role for the Corporation to provide funding to the extent that it was addressing market failures, there was a real risk that the CEFC would in fact end up distorting existing energy and financial markets.

The Association is still cautious about the proposed role for the CEFC for this reason. esaa is supportive of the need for funding to support the process of research, development and demonstration (RD&D) in the energy industry where there are positive benefits which cannot otherwise be captured by those developing the technology. The Association therefore considers that the focus of the CEFC should be on RD&D. However, in terms of providing finance to support deployment projects, there remains a risk of establishing a scheme that will crowd out the private sector and distort existing markets.

Supporting deployment distorts competitive markets

The energy sector as a whole, regardless of the fuel source, faces challenges accessing finance due to a range of commercial and policy reasons. This does not necessarily mean that there are capital market barriers and that the government should intervene in order to provide financing, which is how the CEFC is proposing to operate.

There is, in esaa's view, little justification to support the deployment (as opposed to the earlier stages of development) of renewable energy technologies in Australia's competitive energy markets through the CEFC where there is no demonstrated evidence of market failure.

If the overall objective of creating the CEFC is to reduce Australia's greenhouse gas emissions, then the introduction of a price on carbon into the Australian economy is the Government's main driver to achieve this aim. The carbon price will internalise the cost of greenhouse gas emissions. This enables least cost abatement by the market determining where emissions are most efficiently reduced rather than government schemes to promote particular forms of abatement. Under carbon pricing, renewable energy or low emissions technologies will benefit through their lower or zero greenhouse gas intensity and the projected uplift in energy wholesale prices. However, ultimately the market should be left to determine whether abatement is most efficiently achieved through a shift to renewable energy or through other activities such as reforestation under the Carbon Farming Initiative, energy efficiency or imports of overseas abatement.

In addition, if the Government's objective is to drive the uptake of renewable energy, it already has in place the Renewable Energy Target, which mandates the development of renewable energy generation.

Given the impending carbon price and the RET, there is therefore little rationale for establishing the CEFC if it is "to make investments in businesses and projects in the clean energy sector with the objective of facilitating the flow of funds into the commercialisation and deployment of clean energy technologies," as the *Request for Submissions* document states. Furthermore, providing financing for low emissions technology projects will only serve to crowd out private financing. If it offers funds on concessional terms, the CEFC will be the obvious first point of call for those seeking financing for low emissions projects. Private financing will therefore find it difficult to compete with these terms, and cannot realistically be expected to take on more risk or accept a lower return in order to finance the sector. The resulting subsidy to finance costs may result in distortions to Australia's energy markets: the National Electricity Market, Western Australia's Wholesale Electricity Market and potentially the Renewable Energy Certificate market. By contrast, funding offered on the same terms as the market is prepared to, merely duplicates the role of private finance.

In addition, despite the independence of the CEFC, there is a heavy conflict in the Government's role as investor, regulator, policy maker and technology innovator. This can undermine confidence in a program irrespective of the formal independence of the decision makers from government. Several high profile failures of investments in renewable energy technology companies around the world demonstrate this risk. A rigorous assessment of any proposed project is therefore a crucial part of the CEFC's operation.

Australia's energy sector has undergone a reform process over decades to establish competitive markets underpinned by commercially-based decision making. Interfering in these markets through the use of a distortionary measure such as the CEFC risks undermining the environment for investment in these markets, which are capital

intensive and which generate returns over the lifetime of assets (which may run to several decades).

An important role for governments supporting RD&D

Despite these reservations with the CEFC as a vehicle to support deployment projects, esaa is supportive of funding for the RD&D process to accelerate the development of emerging technologies and considers that the CEFC should be focused on these stages of technology development.

The basic reason why government support for RD&D in energy supply technologies is justified is that RD&D can lead to positive externalities. That is, there are wider benefits from the knowledge created by RD&D that accrue to parties other than those undertaking the RD&D. This means that the social benefit of RD&D is greater than the benefit that can be privately captured, which means the amount of RD&D undertaken by the market, without government support, is likely to be less than the socially optimal amount.

There are several distinct phases in the development of new technologies. The pathway for development begins at the research and development phase where outcomes are highly uncertain. At this phase, the aim is to find technological breakthroughs and reduce costs. Following this, the demonstration phase may be reached where the technology has been proven in practice. At this point, costs are high and public funding is often needed to finance all or part of the costs of the project. As these technologies advance and technical issues are resolved, it is expected that costs will decrease. In this way, funding for RD&D helps to develop technologies to the point where they can begin to be deployed if they are competitive in the market against other technology options.

esaa contends that the CEFC should provide support for energy RD&D rather than for deployment projects as is proposed. esaa sees RD&D as an important part of the transition to a low emissions economy and has developed a set of principles relating to how government should approach support for RD&D. These principles are listed at Appendix A.

Conclusion

esaa remains cautious about the nature of the CEFC and its rationale for providing support. With a carbon price and Renewable Energy Target there seem to be few reasons to justify the CEFC providing support for renewable energy deployment projects unless there is a demonstrated market failure. As the Association has argued however, funding for research, development and demonstration in the energy industry is necessary. Seeing the CEFC invest in these stages of technology development, rather than supporting deployment, would be of greater long-term benefit in progressing towards reducing greenhouse gas emissions.

Any questions about our submission should be addressed to Temay Rigzin by email to Temay.rigzin@esaa.com.au or by telephone on (03) 9670 0188.

Yours sincerely

Clare Savage
Interim Chief Executive Officer

Appendix A – esaa's RD&D principles

1) There is an important role for governments to support research, development and demonstration of stationary energy supply technologies to correct identified market failures.

2) Government RD&D support should clearly articulate its objectives and how it links with energy and other policies.

3) Given the inherent challenges and uncertainties of RD&D, government support must provide a long-term commitment (including support for the different stages of technology development), sufficient resources and be appropriately flexible. Ad hoc programs and arbitrary changes are not conducive to achieving RD&D objectives.

4) Overall, governments should avoid trying to 'pick winners' in energy supply technologies. RD&D policy should be guided by the principle of fuel and technology neutrality.

a. However, individual technologies may necessarily require specific programs which take into account their particular circumstances.

5) RD&D funding programs should not distort existing markets.

6) As Australia is generally a 'technology' taker from the global energy technology market, RD&D programs should focus on:

a. Areas where Australian-specific conditions are particularly relevant to the technology.

b. Supporting Australia to be a 'fast follower' of international technology developments.

7) The energy industry has valuable expertise to contribute to achieving Australia's RD&D objectives. RD&D programs should seek to maximise industry participation.

8) RD&D programs involving industry must recognise the commercial realities businesses face and be designed and administered accordingly. In particular, the RD&D support instrument needs to adequately address the risk/reward balance to make projects commercially justifiable for business.

9) Programs should be designed so as to reflect the differing circumstances of individual technologies. This may be done by:

a. Recognising the specific profile of each technology when designing funding arrangements.

b. Recognising the timing required for different stages of development, so that projects which are ready can begin quickly, and that those which require more data or need to secure funding arrangements can do so without losing their funding.

c. Providing for ongoing or multi-stage funding.

d. Ensuring that funding is targeted appropriately for the scale of the project.

e. Allowing for all relevant technologies to access funding.

10) RD&D programs should be administered effectively and efficiently.

a. Information about programs should be easily available and transparent.

b. Regulatory and compliance costs should be as low as practical.

c. Governance arrangements should be aligned with commercial practices to minimise business compliance costs.

d. There should be coordination where possible between different RD&D programs and different levels of government.