

12 December 2011

Ms Jillian Broadbent AO  
Chair  
Clean Energy Finance Corporation Expert Review  
c/o The Treasury  
Langton Crescent  
PARKES ACT 2600

By email: [cefc@treasury.gov.au](mailto:cefc@treasury.gov.au)

Dear Ms Broadbent

## Clean Energy Finance Corporation Expert Review

Vestas welcomes the opportunity to make a submission as part of the Clean Energy Finance Corporation (CEFC) Expert Review.

Vestas is the world's leading supplier of wind power solutions, having installed more than 40,000 wind turbines across the globe in more than 60 countries.

In Australia we have been responsible for the supply of more than half of the wind energy capacity to date, and we are currently working on Australia's largest wind farms including the 206 megawatt (MW) Collgar project and the 420 MW Macarthur project.

We have a particular interest in the future operation of the CEFC and its relationship with the existing 20% Renewable Energy Target, and are encouraged by the recognition of this issue in section 5 of the Terms of Reference for the Expert Review.

### Allocative efficiency

On many levels the likely entry of \$10 billion of new funding for renewable energy projects holds much appeal. But the way in which this occurs will be crucial.

It is worth reflecting on remarks made by the former Secretary of the Treasury, Ken Henry in a speech on 14 March 2007:

*First, we need to have an appreciation of the consequences of policy intervention in an economy operating at, or close to, full employment. In the absence of externalities and other sources of market failure, a market free of policy intervention will allocate resources efficiently. Any government intervention will shift resources, including jobs, from one activity to another and impose a **deadweight loss of efficiency** on the economy.*

Mr Henry went on to say in the same speech:

*Consider, for example, recent commentary in the press which argues that the Government should support a nuclear power sector because jobs would be created. Where will the nuclear scientists and technicians come from? Is it seriously being suggested that they will come from the dole queue or from Indigenous Community Development Employment Projects?*

*The truth is that if present macroeconomic circumstances persist, unless **all** of the workers employed in the nuclear industry are immigrants who would not otherwise have been drawn to Australia, then every job 'created' by the nuclear industry will be a job 'destroyed' in some other industry. Ignoring transitional cost issues, there is nothing inherently bad about job destruction, of course; but the more important point is that there is nothing inherently 'good' about job creation either, unless it opens up an economic opportunity for someone who would otherwise not have a job or is associated with higher income than the job it replaces. And need I point out that if it belongs to the latter category, then it certainly doesn't need taxpayer support.*

While Mr Henry's 2007 remarks were made in a broader context regarding the Australian economy, his warning about government intervention in a market shifting resources and jobs from one activity to another is highly relevant to the design and activities of the CEFC.

The remarks made by Mr Henry on hypothetical government support for a nuclear power industry in Australia could equally be applied to any support that would be offered by the CEFC for so-called "emerging technologies" in the renewable energy sector.

Those technologies to date have been unsuccessful in reducing their costs to a point where they can take advantage of the Renewable Energy Target (**RET**) legislation, and so their deployment on a large scale has not occurred. In the meantime, however, wind energy investments have begun to flourish.

Many energy sector analysts have forecast that up to 9000 MW of wind energy capacity could be deployed by the year 2020 under existing policy settings, most notably the RET legislation.

Therefore it is highly important that the CEFC design does not distort the existing market for Large Scale Generation Certificates (**LGCs**) to frustrate, delay, defer or displace investments in wind energy that would occur without CEFC involvement.

Doing so would, to use Ken Henry's words, impose a "deadweight loss of efficiency" on the economy.

## Objective/s of the CEFC

The success or failure of the CEFC will be measured against the objective/s it has been charged with achieving.

In the discussion paper for the Expert Review, it is stated:

*The objective of the CEFC is to overcome capital market barriers that hinder the financing, commercialisation and deployment of renewable energy, energy efficiency and low emissions technologies.*

The focus on capital market barriers is welcome. However, it is important that the focus on overcoming these capital market barriers does not interfere with the Australian Government's other objectives in the field of renewable energy.

For example, the Australian Government successfully moved amendments to the *Renewable Energy (Electricity) Act 2000* (also known as **the RET legislation**) in 2009 and 2010 and has made that Act the centrepiece for the achievement of its policy that by 2020, 20% of Australia's electricity should come from renewable sources.

The objectives of the RET legislation are set out in section 3, and are stated to be:

- a) *to encourage the additional generation of electricity from renewable sources;*  
*and*
- b) *to reduce emissions of greenhouse gases in the electricity sector; and*
- c) *to ensure that renewable energy sources are ecologically sustainable.*

In addition, the structure of the RET legislation has a focus on the deployment of renewable energy at the least cost. The way in which the market for LGCs is designed means that the renewable energy generation technology with the lowest long range marginal cost sets the price of LGCs.

The 2010 reforms to the RET legislation were a response to a policy failure where multiple state and federal subsidies for household-scale solar PV panels and solar hot water units, together with the "deeming" provisions of the RET legislation itself had combined to produce such a large glut of Renewable Energy Certificates (**RECs, now known as LGCs**) that this deferred investments in large-scale projects such as wind farms.

## Avoiding distortion of the LGC market

It is important that the design of the CEFC does not have a similar outcome to those state and federal subsidies mentioned above and the damage they did to investments in the wind energy sector prior to the 2010 RET reforms.

While there are plenty of high-cost renewable energy technologies that would no doubt appreciate CEFC support, it would be a poor policy outcome if one of the side-effects of that support was to again defer or displace RET-driven investments in wind energy that would otherwise have taken place in the absence of the CEFC.

One possible way to avoid this market distortion lies in the terms and conditions of the funding agreements between the CEFC and the projects that it loans money to. As a condition of any funding agreement, the CEFC should insist that any LGCs created by a renewable energy project that it loans money to must surrender or assign all LGCs to the CEFC at zero cost. In turn, the CEFC must then surrender these LGCs to the Office of the Renewable Energy Regulator.

The effect of this condition in all CEFC funding agreements would be to preserve the integrity of the LGC market. Any LGCs created by CEFC-backed projects would then be additional to those that met the existing requirements of liable parties under the RET legislation, thus avoiding a distortion of the LGC market and a crash of the LGC price.

The other consequence of such an arrangement would be to avoid the kind of government-driven allocative inefficiency that Ken Henry warned of in 2007. Preserving the integrity of the LGC market allows it to do what it is designed to do; namely, provide a low-cost incentive for the additional generation of electricity from renewable sources.

Structured in this manner, the CEFC then remains free to provide access to funding for whatever high-cost and emerging renewable energy technologies it wishes to support without harming the business case of investors who have chosen to support low-cost renewable energy technologies such as wind power.

### **Next steps**

Vestas staff would be pleased to meet with staff from the Expert Review to discuss our submission and answer any other questions they may have. Please contact the writer on (03) 8698 7300 to do so.

Yours sincerely,

[signed]

**Ken McAlpine**  
**Director, Policy and Government Relations**  
**VESTAS - AUSTRALIAN WIND TECHNOLOGY PTY LTD**