

EXPLANATORY STATEMENT

Select Legislative Instrument 2010 No. 322

Issued by the Authority of the Minister for Climate Change and Energy Efficiency

Renewable Energy (Electricity) Act 2000

*Renewable Energy (Electricity) Amendment (Transitional Provision)
Amendment Regulations 2010 (No. 1)*

Item 15 of Schedule 2 to the *Renewable Energy (Electricity) Amendment Act 2010* (the Act) provides that the Governor-General may make regulations prescribing matters required or permitted by Schedule 2 to the Act, or necessary or convenient to be prescribed for carrying out or giving effect to the Schedule. Item 14 of Schedule 2 provides, in part, that the regulations may deal with matters of a transitional, savings or application nature relating to any of the amendments and repeals made by the Act.

The *Renewable Energy (Electricity) Act 2000* (the Principal Act) as amended by the Act, establishes a Renewable Energy Target (RET) scheme to encourage additional electricity generation from eligible renewable energy sources. The enhanced RET, to commence on 1 January 2011, includes two components - the Large-scale Renewable Energy Target (LRET) and the Small-scale Renewable Energy Scheme (SRES). The RET is designed to ensure that the equivalent of 20 per cent of Australia's electricity supply is generated from renewable sources by 2020.

Under the Principal Act, wholesale electricity purchasers ('liable entities') are required to contribute to the RET in proportion to their share of the national wholesale electricity market. The Principal Act provides for the creation of Renewable Energy Certificates (RECs) by renewable energy generators and in relation to the installation of small generation units and solar water heaters. One REC generally represents one megawatt-hour (MWh) of electricity from eligible energy sources.

The Regulations amend the *Renewable Energy (Electricity) Amendment (Transitional Provision) Regulations 2010* (the Transitional Regulations) to provide an administrative framework to deal with various situations where the enhanced RET legislative changes have affected existing contracts for the supply of RECs.

Background on the policy intent of the Regulations is included in Attachment A. Details of the Regulations is included in Attachment B.

Consultation

In developing these Regulations, the Department of Climate Change and Energy Efficiency conducted a formal stakeholder engagement process. On 7 October 2010 a public exposure draft of the Regulations was released for consultation together with a commentary paper to explain the technical detail of the draft regulations. Stakeholders were invited to make submissions on the draft regulations by 29 October 2010. Feedback received through submissions was considered in finalising the Regulations.

Authority: Items 14 and 15 of Schedule 2 to the
Renewable Energy (Electricity)
Amendment Act 2010

General policy guidance on the *Renewable Energy (Electricity) Amendment (Transitional Provision) Amendment Regulations 2010 (No. 1)*

From 1 January 2011, two categories of RECs will exist – a large-scale generation certificate (LGC) being eligible for surrender under the Large-scale Renewable Energy Target (LRET) but not the Small-scale renewable Energy Scheme (SRES), and a small-scale technology certificate (STC) eligible only under the SRES. The Amendment Act provides that the following RECs are taken to be LGCs:

- all RECs created before the enhanced RET commences (1 January 2011);
- all RECs created by accredited power stations; and
- RECs created (after 31 December 2010) for small generation units and solar water heaters that are installed before 1 January 2011.

This means that from the beginning of 2011, there will be two separate certificate markets under the enhanced RET (one with a floating price, the other with a ‘fixed’ price of \$40) with two sets of certificates. This contrasts with the single, floating price pre-2011 certificate market.

The creation of two categories of certificates through the establishment of the LRET and SRES may create uncertainty around contractual arrangements, entered into before the Government announced the RET enhancements, for the supply of certificates in future years. These contracts place a direct or conditional requirement on one or both parties to buy or sell a quantity of certificates at a specified time and price.

RET-liable parties engage in these contracts to hedge their exposure to future certificate price fluctuations and secure a source of certificates to meet their future RET liabilities. At the same time, they provide the certificate supplier, which could be an accredited power station, a small system supplier or a market intermediary (aggregator/trader), with the security of a guaranteed buyer and price for the certificates it may source, albeit at the risk of forgoing possible higher market prices in the future.

The transfer of certificates from accredited power stations under these contracts does not raise an issue as their use in the floating price LGC market hedges the same exposure as for the pre-2011, floating-price market.

In some cases however, the certificate supplier’s business model may involve sourcing certificates from small-scale systems (for example solar panels or solar water heaters), while the contractual arrangements do not include ‘change in law’ provisions to permit the contract to be terminated or varied when the RET rules are amended.

An issue could arise here, for example where an electricity retailer has entered into a contract in 2009 to purchase certificates in 2013 from a supplier who sources them from installations of solar water heaters. At the time the contract was struck, (before the intent to enhance the RET was announced), it was expected that these certificates could be used to meet any of the liable party’s future RET obligations, avoiding future price risk in the single (floating price) certificate market. However, as a result of the enhancements to the RET, the solar water heater-derived certificates to be delivered in 2013 could only be used to meet the small-scale SRES obligation. While the retailer could use the certificates supplied to acquit its SRES obligation, it would need

to separately purchase certificates on the floating price (LRET) spot market to meet its separate LRET obligation, at a price that could be higher than under the contract. As such, the retailer will have lost the value of the contract as a hedge against the potentially higher prices in the floating LRET certificate market.

If, in addition, the contract price for the certificates in 2013 is greater than the prevailing clearing house price under the SRES (currently \$40), even if used to meet the SRES obligation, the liable entity would forego an amount equivalent to the difference between the clearing house price and the contract price.

To address this issue, item 6 of Schedule 2 to Table A of the Act as amended in June 2010 provides that, where there is no contrary intent in the contract, a reference in the contract to a certificate within the meaning of the REE Act prior to the amendments is taken to mean a reference to the certificate (LGC) under the LRET, even if the certificate is for a small-scale system installation. However, in protecting the liable entity, item 6 shifts exposure to the certificate supplier. For example, where the supplier's business model is to source certificates from small-scale systems, and where the contract does not include change in law provisions, item 6 would effectively force the certificate supplier to provide LGCs rather than the STCs created for solar water heaters. These LGCs, to be sourced through the floating price market, could be at a higher price than the fixed price the supplier would receive for its STCs through the clearing house.

To provide an appropriate mechanism such that the rights of each party to the pre-existing contract are not adversely impacted, item 7 of Schedule 2 to Table A of the Act augments item 6 by enabling small-scale technology certificates (STCs) transferred under pre-existing contracts to become LGCs in prescribed circumstances.

The Act empowers regulations to complete implementation of the policy intent behind the arrangements under items 6 and 7 as described above.

As such, the Regulations establish transitional arrangements for the treatment of certificates where a written contract was entered into before the Government announced its intention to separate the RET into two parts (26 February 2010), and where the contract is for the supply of certificates from 1 January 2011. These regulations reflect the policy intent that only those pre-existing contracts where there is a clear direct or conditional requirement on at least one party to buy or sell certificates. It is not intended that these transitional arrangements would apply to contracts that provide a non-binding option for the transfer of certificates on agreement between the parties to the contract.

The regulations establish a mechanism where either party to a contract that meets the requirements of sub-item 7(1) of Schedule 2 to Table A of the Act may apply to the Regulator to have their contract recognised as one where some or all of the STCs transferred under the contract may become LGCs. In summary the regulations:

- clarify the interpretation of references to 'renewable energy certificates' in contracts;
- prescribe a process, including timing and information/documentation requirements, whereby a party to a relevant contract may apply to the Regulator for consideration of an annual allocation of certificates for conversion from STCs to LGCs;
- prescribe a process for the Regulator to estimate the annual allocation, consult with other parties to the contract, and determine the final amount of the allocation;
- prescribe a process for review of the Regulator's determination; and

- prescribe a process for a party to a contract to then apply for certificates to be transferred under the contract to become LGCs.

The regulations also prescribe that the Regulator must publish on its website the aggregate of the annual allocations for each year, before 1 April 2011.

Details of the *Renewable Energy (Electricity) Amendment (Transitional Provision) Amendment Regulations 2010 (No. 1)*

Regulation 1 – Name of Regulations

Regulation 1 states the title of Regulations is the *Renewable Energy (Electricity) Amendment (Transitional Provision) Amendment Regulations 2010 (No. 1)*.

Regulation 2 – Commencement

Regulation 2 states the commencement of the Regulations is the day after registration on the Federal Register of Legislative Instruments.

Regulation 3 – Amendment of *Renewable Energy (Electricity) Amendment (Transitional Provision) Regulations 2010*

Regulation 3 notes that Schedule 1 to the Regulations amends the *Renewable Energy (Electricity) Amendment (Transitional Provision) Regulations 2010* (the Principal Regulations).

Schedule 1 – Amendments

Item 1 – Before regulation 1

This item inserts the title ‘Part 1 – Preliminary’ into the Principal Regulations before regulation 1.

Item 2 – Regulation 1

This item amends the name of regulation 1 in the Principal Regulations *Renewable Energy (Electricity Amendment (Transitional Provisions) Regulations 2010*.

Item 3 – After regulation 2

Regulation 2A – Definitions

This item inserts a new regulation 2A, including three definitions; two clarifying references to the *amending Act* and the *principal Act* and the third to specify that the *annual transfer number* is defined by subregulation 8(2).

Item 4 – Before regulation 3

This item inserts a new title for Part 2 of the Principal Regulations.

Item 5 – Regulation 3, heading

This item substitutes the heading for regulation 3 to clarify these regulations deal with solar water heaters.

Item 6 – Subregulation 3 (1)

This item clarifies a reference to the amending Act and principal Act in existing subregulation 3(1).

Item 7 – Subregulation 3 (2), definition of *acquirer*

This item clarifies a reference to the principal Act in the definition of *acquirer* in existing subregulation 3(2).

Item 8 – Subregulation 3 (2), definition of *Act*

This item deletes the definition of *Act* in the Principal Regulations.

Item 9 – After regulation 3

This item inserts new regulations 4 and 5 into Part 2 and a new Part 3, including new regulations 6 to 15, as outlined below.

Regulation 4 – Publication of renewable energy certificate shortfall information

Regulation 4 clarifies that the amendment in the Act relating to the publication of information relating to the shortfall charge under the LRET and the SRES does not apply in relation to the shortfall charge under the RET before 2011. The amendment is intended to clarify that information on the shortfall charge for the operation of the RET scheme up to 31 December 2010 would still continue to be published.

Regulation 5 – References in contracts to renewable energy certificates

Regulation 5 specifies that relevant contracts for the purpose of certificates being considered LGCs (under paragraph 6(3)(c) of Schedule 2 to the Amendment Act) are contracts specifically relating to the supply or transfer of certificates from 1 January 2011.

Paragraph 5(2)(a) specifies that the provision would not apply to contracts entered into after the Government announced its intention to separate the RET and where the contract describes certificates as 'small-scale renewable energy certificates' which was the term originally used in relation to the changes.

Paragraph 5(2)(b) also does not apply to contracts that would, but for the enactment of item 6 (of the Amendment Act), have otherwise terminated as a result of the amendments. For instance, without the deeming in item 6, a contract may have terminated through a change in law provision but the operation of item 6 is sufficient to avoid that termination circumstance. This ensures that item 6 does not undermine the original termination provided by the contract.

Similar to paragraph 5(2)(b), subregulation 5(3) deals with contracts which provided a right to terminate but did not actually terminate of their own accord from the amendments (other than item 6). In these circumstances, the election to terminate must be communicated to the Regulator and each other party to the contract.

Subregulation 5(4) specifies that the provision would not apply to contracts entered into after the Government announcement on 26 February 2010 of its intention to separate the scheme and the Royal Assent of the enhanced RET legislation on 28 June 2010 where the contract was for the transfer of certificates from small-scale technologies after 1 March 2011. This is because such contractual arrangements will not be able to benefit from the arrangements flowing from Item 7 (of the Amendment Act) or be able to use the ability to create LGCs from installations prior to 1 January 2011 to satisfy the contractual obligation to transfer LGCs.

Part 3 – Transitional - transfer of certificates taken to be large-scale generation certificates

Regulation 6 – Application

Regulation 6 clarifies that Part 1 of the Principal Regulations relating to the transfer of certificates taken to be LGCs is made for subitems 7(2) and (3) of Schedule 2 to the Amendment Act.

Regulation 7 – Annual transfer number – applications

Regulation 7 specifies the contents of an application from a party to a contract seeking to have some or all of the certificates from small-scale technologies under that contract recognised as eligible to be transferred as LGCs rather than STCs.

The regulation allows a party to an eligible contract for the future supply of certificates to apply to the Regulator to have a certain number of certificates transferred under the contract each year (the annual transfer number) to be considered LGCs. In particular, the annual transfer number will set an upper limit on the number of STCs that may become LGCs for the year to which it applies. A contract may only have one annual transfer number (e.g. just for 2011) or may have multiple (e.g. one annual transfer number for 2011 and another for 2012).

The application would need to be made prior to the commencement of the enhanced RET, that is, before 1 January 2011. Subregulation 7(4) provides that the information in the application would need to be verified through a statutory declaration.

The regulation outlines the details to be included in the application for an annual transfer number, including a statement that the contract is eligible for such an application by way of subitem 7(1) of Schedule 2 to the Amendment Act, and the circumstances that the applicant considers make the contract eligible.

The application is also required to include documentation to support the application, including a copy of the contract itself, any document incorporated into, or referred to by, the contract and any other document relied upon to show that subitem 7(1) applies to the contract. In particular,

the documents will need to establish why the party considers that the contract refers to the certificates as being created in relation to solar water heaters or small generation units or show that it is clear from the context of the contract that the party expects the certificates to be created for installations of solar water heaters or small generation units. In some cases eligibility may be clear on the face of the contract, in other cases more detailed materials and documentation may be required.

The applicant is required to state in the application the total number of certificates transferred under the contract (or under other contracts or arrangements) in previous years (2008, 2009 and 2010), the date of transfer and the source of the certificates (from small-scale technologies or power stations). This would assist the Regulator in assessing the history of the number of certificates that would usually have been transferred under the contract, estimate the proportion that would have been created from small-scale technologies, assess the likelihood that they would otherwise be supplied as STCs in future years and understand the volumes of certificates that are likely to be transferred between the parties if this was not specified in the contract.

The application must also specify the certificates to be transferred under the contract from 1 January 2011 that are expected to be created in relation to small-scale technologies installed after 1 January 2011 or in relation to installation before 1 January 2011 or created in relation to accredited power stations. This is intended to address issues with contracts where there was an intention to supply certificates that would already be considered LGCs. For instance, most transfers prior to 14 February 2011 will be for certificates with a 2010 'generation year' or earlier as these are the only certificates that may be used for 2010 liability. It is also unlikely that certificates created from small-scale technologies installed after 1 January 2011 would have necessarily been validated in time for transfers before 14 February 2011. It is also intended to address contracts where accredited power stations certificates might also be used.

Regulation 8 – Annual transfer number – Regulator's estimate

Regulation 8 outlines how the Regulator would estimate an annual transfer number once an application has been received in accordance with Regulation 7. Subregulation 8(2) provides a rule for determining an annual transfer number in two situations.

Case one

In the first situation, there may be a contract between a seller and buyer of certificates that was in force before 26 February 2010 and includes a schedule that states a fixed number of certificates to be transferred in the future. In this situation, the estimated annual transfer number is the number of certificates the Regulator considers would, but for the enactment of the Amendment Act, have been transferred under the contract subject to subregulation 8(3). Under subregulation 8(3), the Regulator would disregard certificates that are expected to come from solar water heaters or small generation units installed before 1 January 2011 (which will be LGCs from 1 January 2011) or from accredited power stations (as these will be LGCs from 1 January 2011).

For example, a contract executed on 1 January 2010 may exist between an installer of solar water heaters (the seller of certificates) and an ‘aggregator’ of certificates (the buyer) that sources certificates on behalf of a RET liable entity, which states that 100,000 certificates would be transferred on 30 April 2011 and a further 100,000 certificates would be transferred on 31 August 2011. Unless proposed subregulation 8(3) applies, which requires the Regulator to disregard certificates in relation to systems installed before 1 January 2011, the estimated annual transfer number for 2011 would be 200,000.

Alternatively a contract may exist between an aggregator of certificates (the seller in this example) and a RET liable entity such as an electricity retailer (the buyer) and may include an agreement to provide 500,000 certificates of which 50 percent were to come from solar water heaters and small generation units and 50 percent were to come from accredited power stations such as wind farms. In this case, the Regulator would estimate the annual transfer number to be 250,000 certificates as the certificates to come from the wind farms must be disregarded (these are automatically LGCs from 1 January 2011).

Case 2

The second situation could occur where there is a clear direct or conditional requirement on one of the parties to the contract. As for case 1, the policy intent is to ensure that pre-existing property rights inherent in the contracts are not interfered with.

For example, this could occur where the number of certificates to be transferred from the seller to the buyer may be dependent upon an external variable (such as a multiple of the renewable power percentage or when a ‘spot’ market price for certificates reaches a particular price point) or where the seller is required to transfer a number of certificates specified by the purchaser which is within a range (e.g. a purchaser may specify a number between 10,000 and 20,000 certificates).

In this situation a range of factors may be considered by the Regulator in determining the number of certificates that would have been transferred under the contract had the amendments (including the split scheme) not taken place. For instance, if historically the number of certificates transferred was consistently toward the lower end of the range, this would indicate that that behaviour would have been likely to continue. However, contrary evidence could be provided by the parties to indicate that they would have enlarged the volumes in the circumstances where the pre-amendment regime continued.

Subregulation 8(3), as referred above, specifies that in making an estimate of the annual transfer number, the Regulator is to disregard certificates that are expected to come from solar water heaters or small generation units installed before 1 January 2011 (which will be LGCs) or from accredited power stations (as these will be LGCs). The relevant time to consider this expectation is at the time the contract was entered into.

Subregulation 8(4) provides a particular rule for transfers before 15 February 2011 which are taken to be in relation to LGCs unless a party to the contract proves to the contrary. This is

because only certificates which are LGCs are able to be used to meet 2010 liability and this is assumed to be a key reason why a party would require certificates before 15 February 2011. Additionally, it is very unlikely that installations after 1 January 2011 would have STCs created and validated by the Regulator in time for transfer to a third party before 15 February.

Regulation 9 – Estimated annual transfer amount – consultation

Regulation 9 outlines the process for consulting with the parties to the contract, after the Regulator receives an application for an annual transfer number. In particular, the Regulator is required to provide a copy of the application to the other parties to the contract and provide an opportunity for them to comment. The Regulator is also required to provide all parties to the contract with its estimate of the annual transfer number and provide an opportunity for comment. If the Regulator considers that subitem 7(1) of Schedule 2 to the Amendment Act does not apply to the contract, the Regulator could also make this clear in the invitation for comment. Nonetheless, this issue may also arise in light of consultation and the Regulator may need to seek additional comments from the parties to ensure natural justice is afforded before a final decision is made.

The parties will have 30 days to respond to the invitation in writing.

Regulation 10 – Annual transfer number – Regulator's determination

Regulation 10 establishes the process for the Regulator's decision in relation to an annual transfer number application. In particular, the Regulator is required to make a determination as to whether the contract was eligible for an annual transfer number and if so, determine the annual transfer number for each year and advise the parties to the contract of that determination.

Subregulations 10(2) and 10(3) mirror the tests in subregulations 8(3) and 8(4) and are intended to be interpreted consistently with those subregulations.

In making its determination, the Regulator is required to take into account any comments from the parties to the contract provided during the consultation process, including any proof to the contrary in relation to certificates expected to be transferred.

The Regulator's decision will also set an identification number to be used in respect of that contract and the transfers under it.

Regulation 11 – Review of Regulator's determination

Regulation 11 outlines the process for the Regulator to reconsider their determination where a party to a contract seeks a review of the determination. The regulation also specifies that applications for review of the Regulator's determination could be made to the Administrative Appeals Tribunal. This review process mirrors that provided for in section 66 of the Act.

Regulation 12 – Publication of aggregate annual transfer number

Regulation 12 requires the Regulator to publish on its website the total number of certificates eligible for transfer each year under its annual transfer number determinations. This must be published before 1 April 2011.

Regulation 13 – Request for certificates to become large-scale generation certificates

Regulation 13 establishes the process for requesting STCs transferred under an eligible contract to become LGCs where an annual transfer number determination has been made by the Regulator.

This regulation sets out the requirements for the application, including the number of certificates to be transferred and when they will be transferred, as well as a requirement that the application be accompanied by a statutory declaration. The application is also required to include the identification number for a contract.

Regulation 14 – Inclusion of certificates in the register of large-scale generation certificates

Regulation 14 establishes the requirements of the Regulator to register eligible certificates transferred under a relevant contract on the register of LGCs. In particular:

- the number of certificates must not exceed the annual transfer number for the year;
- the contract must remain in force (such that it is not terminated, suspended or otherwise invalidated);
- the contractual requirement existed before 26 February 2010 (such that it is not pursuant to an amendment to the contract after that date, however a requirement which existed before 26 February but was dependent on a subsequent trigger would still qualify);
- the STCs are additional to any LGCs which are being transferred to meet the requirement (e.g. if 10,000 certificates are needed and 5,000 LGCs have already been transferred, only 5,000 STCs could be eligible); and
- the certificate must not have been acquired through the clearing house.

Subregulations 14(3) and (4) require the Regulator when including transferred certificates on the register to include information to identify the specific certificates and to notify the parties to the contract of the registered certificates.

Regulation 15 – Conversion of certificates to large-scale generation certificates

Regulation 15 outlines that the point at which a certificate transferred under an eligible contract for the purpose of annual transfer becomes, and is taken to have been, an LGC is when the certificate is added by the Regulator to the register of LGCs.