27 April 2020

Victorian Government Department of Environment, Land, Water and Planning
By email: lily.dambrosio@parliament.vic.gov.au

(Please redirect as necessary to the appropriate person)

Dear Sir/Madam,

Shocks to the Victorian Energy Efficiency Certificate scheme market

We are writing to raise with you concerns that have been expressed to us by our member firms in relation to the combined impact of COVID-19 and upcoming regulatory changes on the Victorian Energy Efficiency Certificate scheme (VEEC) market.

The Australian Financial Markets Association represents participants of Australia's primary formal trading markets. We are an authority on market efficiency and market-based policy development. We also convene a committee with common interests in traded environmental certificates and schemes. The member companies include the following parties, many of whom participate in the Victorian VEEC scheme:

- AGL Energy
- Origin Energy
- EnergyAustralia
- ANZ
- CS Energy
- ERM
- Engie
- Hydro Tasmania
- Macquarie Group
- Snowy Hydro
- Ergon Energy
- Stanwell
- ICAP brokers
- GFI brokers

Our members are starting to see the COVID-19 pandemic impact the supply of Victorian Energy Efficiency Certificates. At the same time, we expect to see demand for certificates to grow substantially, particularly if changes to the Victorian Energy Upgrades program are implemented as proposed. The resulting imbalance from this tightening of supply would lead to market distortion and artificial price increases that are unnecessary and should be avoided. Accordingly, we request that you consider implementing some liability relief and defer implementation of currently proposed policy changes to provide a smoother transition period for the market.

The Victorian Government has suspended VEEC scheme installations that would normally occur within occupied premises. We support this move as it will reduce the risk of COVID-19 spread in the community. We note that the suspension impacts several categories that produce certificates; incandescent lighting upgrades (Part 21 under the Victorian Energy Efficiency Target Regulations 2018), low-flow shower roses (Part 17), weather sealing (Part 15), and in-home display units (Part 30). These categories had supplied over 70% of the market's VEECs. Irrespective of this suspension, it is the opinion of some member organisations that some home occupants and businesses may have become hesitant to let installers enter their premises to complete installations, and so the volume delivered to market was already trending down. Further, we note that supplies of some stock and materials had already been constrained by the impacts of COVID 19 on international supply chains.

Buyers and sellers of forward-sold certificate volumes have naturally been the first to sound the alarm. Sellers recognise that they will be unable to meet the volumes promised under their contracts and face the prospect of having to pay their counterparties the penalty price for the shortfall. This might push smaller suppliers towards financial distress. Buyers will increasingly face incomplete certificate inventories to surrender when they are due early next year, will carry higher costs and in turn pass through higher costs to their own customers at a time that electricity customers aren't well equipped to absorb them.

We ask that you consider some liability relief to ameliorate demand-side pressures and support buyers to offer more flexible terms to their suppliers in response to the Pandemic.

These very recent challenges compound existing disruption to the market that caused escalation in the traded price of VEECs before Christmas. This disruption comes as the market braces for regulatory changes that were outlined by the Department in the Victorian Energy Efficiency Target (VEET) Amendment Regulations 2020 Regulatory Impact Statement (RIS), and the Victorian Energy Upgrades Lighting Activities Issues Paper. The changes outlined in these papers may cause significant shock to the market even in the absence of COVID-19 and should now be approached only with caution and with a commitment to ease transition periods.

In addition to recommending that liable entities must buy and surrender more VEECs, the RIS and Lighting Issues Paper propose changes to the market that would compound the existing supply-side shock, including:

- A sharp step down in the 10-year forward average emissions factors, which act as multipliers for the number of energy efficiency upgrades required for each year
- Increased penalty rates from $50 to $112
- Phase out, beyond what has already resulted from COVID-19, of certificates generated for the installation of energy efficient lighting, equivalent to over 90% of recent VEEC creation, before replacement technologies are accredited and deployed into the market.

Taken in combination, these changes would require installers to make more installations from a dramatically reduced pool of technologies and for the same number of certificates and would increase the cost and liability for buyers at a time when the market is contracting.

Given the size of the shock we are already seeing, we would recommend deferring policy changes that would overlay additional restrictions on the supply side and costs on the demand side. We would counsel that layering changes that each present a shock to the market would risk the functioning of the market itself. Rather, we recommend a more gradual approach that resolves the supply side of the scheme before making changes to the demand side and emissions factor. One potential solution to this problem is to implement a carry – over mechanism for liable parties similar to that in place under the federal LRET scheme. This would allow demand to be deferred to future years whilst still obliging liable parties to meet demand. Critically, replacement abatement methodologies should be approved and given time to mature in the field before other scheme parameters are adjusted.

We wish you and those close to the VEEC scheme the very best through these difficult months and would be pleased to discuss our comments should that be useful. We look forward to more stable days for our key markets and members.

Yours sincerely

Mike Chadwick
Head of Education and Director-Markets