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RUSAL Australia submission to the COAG Working Group On Climate Change and Water Discussion Paper on Design Options for the Expanded National Renewable Energy Target

RUSAL Australia is an equity participant in the Queensland Alumina Refinery located at Gladstone. RUSAL Australia makes the following observations in response to proposed expansion of national Mandatory Renewable Energy Target.

RUSAL Australia does not support an expansion of the existing MRET. Like the proposed ETS system due for introduction in 2010, an expanded MRET will seriously damage export and import-competing industry competitiveness. The development of these two Government policies as parallel measures rather than an integrated response is concerning. Both the RET and ETS policy proposals have serious and long term impacts for the energy intensive and trade exposed sectors of the economy that prejudice existing investments and put at risk the sustaining capital investments required for continued efficient operation of facilities. Emissions and economic activity will move offshore with potentially higher global emissions levels. Similarly jobs will disappear locally and new job opportunities will also move offshore with the emissions. In summary the carbon leakage resulting from the proposed policies will be destructive for jobs, destructive for existing and new investment and destructive in terms of global energy efficiency and abatement opportunities.

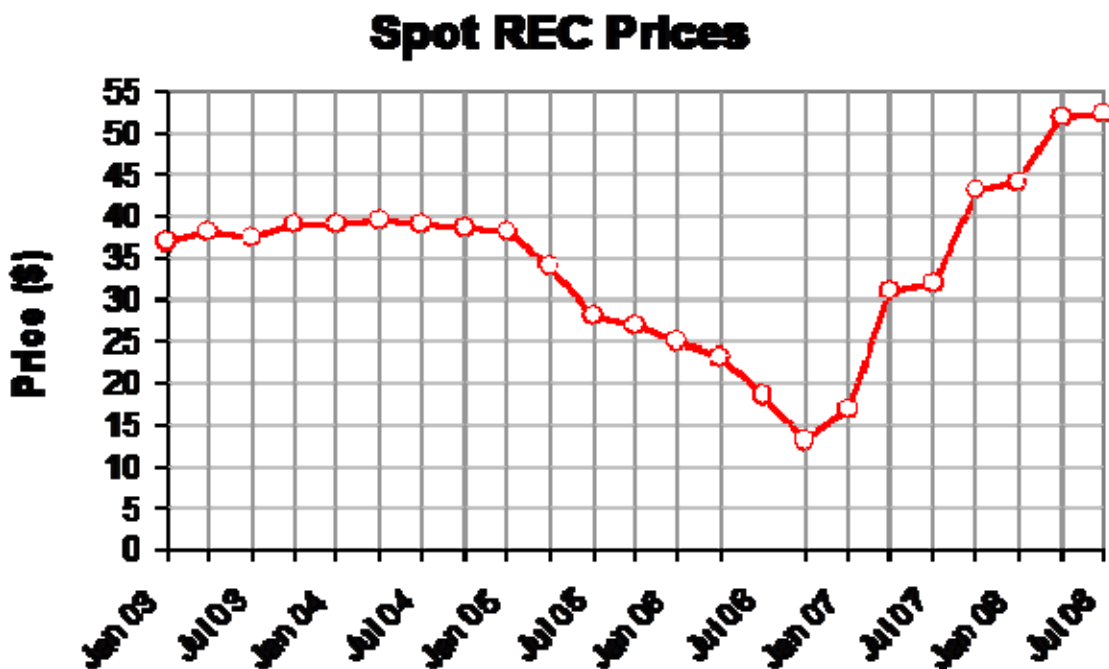
The expanded (M)RET 45,000GWh target will be costly even with the penalty price cap of the existing MRET scheme (\$57post tax). However RUSAL Australia has serious doubts that the higher target can be met by the nominated 2020 timeframe without a substantially higher penalty. The company is also concerned by the large "hidden" market costs for back-up generation capacity for non-scheduled renewable generation. We also believe there is a major risk that the artificial REC market (fixed demand, variable price) will be dysfunctional and unstable and easily manipulated as is the case in the existing market.

RUSAL Australia believes the substantive issues to be addressed by government should include:

Windfall Profit to Existing MRET Generators

A simple increase of the existing Mandatory Renewable Target scheme that allows registered generators to sell Renewable Energy Certificates (RECs) into an expanded REC market will result in large windfall profits for generators without any additional abatement of emissions. In summary:

- The generation required to meet the existing MRET target of 9,500 GWh per year (by 2010) has essentially been built
- The spot value of RECs produced under the MRET scheme fell to below \$20 in late 2006. The expectation of an expanded RET has caused withholding of RECs and gaming of the market towards the effective maximum price under the scheme. (See REC spot prices chart)



- Essentially, existing generators believe that banked RECs will be sold at a higher price into an expanded RET market.
- This price increase will result in no emissions reduction from existing generation, but a massive cost increase to consumers. If we assume 75% of the production is not hedged from 2010 to 2020, and the new RET market causes a REC price increase of \$30, then consumers will pay \$2.4 billion for zero reduction in emissions over this period.

Recommendations

REC market gaming has been caused by the assumption of the renewables industry that RECs from existing generation will be fully fungible in the expanded RET market. Rusal believes this problem must be addressed to ensure cost-efficient carbon abatement under the expanded RET scheme.

These windfall profits could be avoided by applying a conversion factor to the output from existing registered generation such that this output has a reduced number of certificates in the new RET market.

For example if modelling indicates that the price in the expanded REC market ('REC2') will be \$60, an effective REC price of \$20 for existing generation will be obtained if:

1. Existing generators obtain 1 'REC2' from 3MWh of generation (rather than 3 RECs).
2. The first 6,333GWh (i.e. 2/3 of 9,500GWh) of the expanded RET target of 45,000GWh is assumed met. That is, 38,667 'REC2's are required in 2020 to meet the 45,000GWh target.

This method can also be applied to other state-based schemes to avoid windfall profits for existing generators.

Carbon Emissions Permits or Trading

It is government policy to introduce a carbon emissions trading scheme in the period 2010

It is RUSAL Australia's understanding that the government plans to reduce the direct subsidy to renewable generators as carbon costs increase for competing fossil-fuelled generation. This will ensure the renewable generators are not gifted windfall profits in the expanded RET scheme.

RUSAL Australia strongly supports the reduction in the cost of a RET scheme as the price of carbon increases the costs of competing generators and thus price in the electricity market.

RUSAL Australia notes this position was also assumed by Renewable Energy Generation of Australia in the modelling they commissioned from McLennan Magasanik Associates to lobby for an expanded RET^[1].

Avoiding The Double Tax Impact of RET

To avoid the wrong policy outcomes the RET REC price cap should be reduced by the increase in electricity prices caused by the carbon market. This would be recalculated each year. All consumers would benefit from not paying carbon double-taxation.

RUSAL Australia would be pleased to have an opportunity to expand on its views on these issues. This is particularly important for the company as it considers it's future investment profile and planning for Australia.

Yours faithfully



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Chairman
RUSAL Australia

^[1]McLennan Magasaniks Associates & CoPS, "Increasing Australia's Low Emission Electricity Generation - An Analysis of Emissions Trading and a Complementary Measure" 24 October 2007
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