4 December 2023

Hydrogen Strategy Team
Office of Energy and Climate Change
NSW Treasury

Submitted via email

Dear Hydrogen Strategy Team,

NSW Renewable Fuel Scheme- discussion paper on scheme expansion

The Australian Financial Markets Association (**AFMA**) is providing the requested feedback on the discussion paper regarding potential expansion of the NSW Renewable Fuel Scheme (**the RFS**).

AFMA is the leading financial markets industry association promoting efficiency, integrity and professionalism in Australia's financial markets, including the capital, credit, derivatives, foreign exchange, energy, carbon, and other specialist markets. Our membership base is comprised of over 125 of Australia's leading financial market participants, including many of the key participants in Australia's natural gas and enviromental product markets.

AFMA supports the legislated 2050 net-zero target and acknowledges that this will require significant change in the energy sector. In building the next generation of assets and technologies, the transition will require sizeable and regular capital inputs from the private sector. Renewable fuels are likely to play an important role in the transition but AFMA believes that markets will play determining which fuels are most suitable. AFMA therefore adopts a technologically/ fuel neutral stance because we understand that markets will naturally drive the most efficient asset and technology outcomes. On this basis, AFMA supports the proposal to expand the RFS to include other renewable fuels, beyond hydrogen.

The proposals in the discussion paper amount to a fundemental redesign of the RFS which we think will be challenging to I plement by 2025. We understand that the Government intends to implement the RFS as a hydrogen only scheme in 2025 and consider expanding it in future years, we do not think this is desierable and suggest delaying the scheme until all fuels can be included.

Key points

- AFMA supports:
  - expanding the RFS to include other renewable fuels
  - aligned it with the Commonwealth REGO and GO schemes
- Fuel specific incentives should be avoided as markets naturally determine costs and support the expansion of the most commercially viable fuels.
- Costs associated with the RFS should be borne by those who benefit from it.
- Implementation of the RFS should be delayed to allow more renewable fuels to be included.

1. RFS commencement

As you have identified the proposed changes to the eligible fuels and liable entities are quite significant and are unlikely to be able to be implemented by 2025, but we do not support commencing the RFS in 2025 with only hydrogen included as a renewable fuel. Certainty about the RFS is essential to allow it to provide effective market signals that will encourage investment in renewable fuels. We think commencing as a hydrogen only RFS but with a clear indication that other fuels are likely to be added in future is problematic as investors in both hydrogen production facilities do not have certainty that there will be continued demand for their product once when other fuels are added. We therefore think it would be preferable to delay implementation until the details of the role other fuels will play in the RFS is clearer.

AFMA Recommendations
i. Implementation of the RFS should be delayed to allow more renewable fuels to be included.

2. Fuel expansion

While we appreciate the NSW Hydrogen Strategy's ambition, as we recently highlighted in our submission to the Commonwealth National Hydrogen Strategy Review,[1] the green hydrogen industry is embryonic and is not in a position to supply meaningful volumes of fuel. Therefore, AFMA supports the proposed expansion of the RFS, beyond hydrogen, to other renewable fuels. As noted in the discussion paper, a range of fuels will be critical to achieving our 2050 target and AFMA believes that including an expansive range of fuels in the RFS will aid these efforts. As also expressed in the discussion paper, renewable fuels are in the early stages of development and are not yet const competitive with existing fuels; we believe that allowing different renewable fuels to compete will lead to the lowest cost.

It is our assessment that as we move through the transition, the market will naturally determine and drive investment into the most efficient, economic, and long-term viable fuel. By that same merit, with regard to the question of incentives, AFMA would discourage government from pursuing fuel specific incentives as we consider markets naturally determine costs and support the expansion of the most commercially viable fuels.

As part of RFS expansion, for transparency, commonality, compliance, and environmental integrity purposes, AFMA would recommend aligning with the Guarantee of Origin Scheme (GO) and Renewable Electricity Guarantee of Origin (REGO). Noting the Government's concern regarding safeguarding environmental outcomes, AFMA believes that such alignment will be pivotal. Ensuring transparent information about price and volume for all renewable fuel transactions that benefit from the RFS will also aid market participation and growth. Similarly, we also believe that relying on the GO scheme's register to verify, will simplify administration of the RFS and ease the compliance burden for liable entities.

AFMA Recommendations
ii. Expand the RFS to include other renewable fuels.
iii. Align with the GO and REGO Schemes.

3. Liable party expansion

[1] AFMA submission, 18 August 2023, National Hydrogen Strategy Review

As we argued in our previous submission, AFMA's view is that the cost of the RFS should be borne by the entities that benefit from it. Our understanding is that, at least in its early stage, the RFS is unlikely to deliver significant volumes of renewable gas to distribution connected gas customers and therefore it is unclear to us why retail gas customers should bear the majority of the cost. We therefore support expanding the scope of liable parties to the emissions intensive industries that are likely to be the main beneficiaries of the RFS, such as the automotive gasoline industry, diesel industry and aviation fuel.

AFMA Recommendations

iv. The cost of the RFS should be borne by the sectors that benefit from it most, therefore AFMA supports expanding the liable parties to other emissions intensive industries that will benefit from the RFS.

4. Target design

Whilst our comments on target design are dependent on the detailed design of the target, we believe that target option 1, a single fuel agnostic target, is the optimum approach. As highlighted above, we support fuel neutral stances as we consider that allowing different renewable fuels to compete in the market will lead to the lowest cost. As also highlighted in the discussion paper, option 1 maximises cost-effective short-term emissions abatement and provides greater simplicity in the RFS design. As you may recall from AFMA's previous submission, we view RFS simplicity, alignment, and simplified compliance as important to the RFS's success. We therefore believe that the target should not seek to support or incentives any particular fuel.

Nonetheless, in the event that government opts to pursue option 3, a single target with certificate multiplier for hydrogen, AFMA sees both risk and opportunity in this option. There is potential for the market to become liquid and the certificates fungible, but if the hydrogen multiplier is too high, it could undermine and crowd out the rest of the market. AFMA is also concerned that this approach would also cloud the ability to assess and measure impact on the target, due to the multiplier effect. Creating a workable hydrogen multiplier design would be a technical challenge and less workable. Given that certificate creation within the GO scheme is based upon carbon intensity and with the goal of emissions reduction in mind; we believe that carbon intensity could form the basis for the multiplier.

AFMA considers that the actual target needs to strike a balance between providing the market with certainty but retaining sufficient flexibility to accommodate the changing nature of energy usage. We anticipate this will be particularly challenging as the nature of energy demand is changing quite rapidly making it very difficult to predict gas demand throughout the lifetime of the RFS. Our members' preference is for a clear initial target in gigajoules, with allowance for a future review of the target to allow it to be adjusted to accommodate developments in the market.

AFMA Recommendations

v. Implement a single fuel agnostic target.
vi. The target should be expressed in gigajoules.
vii. There should be a review of the target 5 years after the commencement of the RFS.

AFMA would welcome the opportunity to discuss this submission further and would be pleased to provide further information or clarity as required. Please contact me via myoung@afma.com.au or 02 9776 7917.

Yours sincerely,

Monica Young

Policy Manager