



New Indonesian feed-in tariffs: Will renewables benefit?

Energy Alert

7 Mar 2017

By: Michael Horn | Andhari Sidharta

In January 2017, the Indonesian Minister of Energy and Mineral Resources introduced new feed-in-tariff (FIT) and procurement schemes for a range of renewable energy sources. The Minister issued a new renewable energy regulation, Regulation 12/2017 on the Use of Renewable Energy for the Provision of Electricity (Regulation 12). Regulation 12 will lower tariffs paid to private developers, causing some projects to become commercially unviable, but arguably encourages Indonesia's state-owned utility company PLN to purchase electricity from renewable energy sources by lowering PLN's financial burden through indexing all renewable energy tariffs to PLN's local production costs.

Under Regulation 12, all renewable energy tariffs (except for geothermal and waste projects¹ and projects where procurement using direct selection method is used²) will be capped at 85% of the local production cost (locally known as the BPP) if the local production cost is higher than the national average production cost. If the local production cost is the same or lower than the national average production cost, then the reference price will be 100% of the local production cost. The regulation is unclear as to whether 100% is a cap or a fixed amount.

This approach means that certain regions in the country may enjoy higher FITs than other regions if PLN's local production costs are higher, although the attractiveness of this may be limited by the discount imposed by the 85% cap. Currently, the national average production cost in Indonesia is around Rp. 1,400 (USD 0.12) per kWh, while local production costs vary from region to region. For example, the current local production cost in Papua is around Rp. 2,500

(USD 0.21) per kWh, while in Java the cost is around Rp. 800 (USD 0.06) per kWh.

Regulation 12 does not apply to power purchase agreements (PPAs) that have already been signed. In this case, the signed PPA pricing terms will remain in effect. If a PPA has not been signed but the developer has been designated as the project developer by either the Government or PLN, the pricing will follow the provisions of Regulation 12. There is one exception, however, for geothermal projects. If a geothermal developer has not signed a PPA but has won the auction for the concession in accordance with the existing legislation, the tariff to be used will be the tariff stipulated by the developer in its winning bid and the new FIT for geothermal projects will not apply.

The FIT mechanism under Regulation 12 has so far received mixed responses from the business community. Some feel that the current FITs unfairly disadvantages renewable energy producers, as the FITs stipulated under the previous regime were generally higher than the local production costs. The current FIT mechanism therefore might slow down investment activities in the sector, which would not be an ideal scenario given that a number of provinces in Indonesia (particularly those in the eastern region) have suffered from rolling blackouts causing losses to local businesses. The province of Papua, for example, had an electrification rate of 45.93% in 2016, much lower than the electrification rate of more developed provinces. By comparison, in 2016 Central Java had an electrification rate of 91%, and the national electrification rate was around 85%.

Others believe that, by limiting what PLN will pay, Regulation 12 will be an effective tool to encourage PLN to issue tenders for renewable energy projects and purchase more electricity from renewable sources. PLN has been reluctant to purchase electricity from renewable energy producers, claiming that the FITs under the old regime were too high and citing its difficulty in obtaining subsidies from the State Budget. In the 2017 State Budget, some electricity subsidies, including a renewable energy subsidy, were removed. The National Energy Board originally recommended a Rp. 1.2 trillion (USD 89.2 million) renewable energy subsidy, but this proposal was rejected by the House of Representatives. The lower FIT levels provided in Regulation 12 are therefore in line with the central government's intention to reduce and eventually cut retail electricity subsidies for PLN.

Regulation 12 also sets out the procurement methods to be used by PLN in sourcing electricity from renewable energy producers, as summarized in the table below.

Renewable Energy Type	Procurement Method
Wind	Auction to award capacity
Hydro	Either reference price ³ or direct selection ⁴
Solar PV	Auction to award capacity
Biomass	Reference price (for projects with 10MW capacity or less) or direct selection (for projects with more than 10 MW capacity)
Biogas	Reference price (for projects with 10MW capacity or less) or direct selection (for projects with more than 10 MW capacity)
Geothermal	Reference price
Waste	Reference price

The use of auctions to award solar capacity introduces price bidding as a factor in competitive tenders, and replaces the existing system of first come/first served allocation of capacity quota at a fixed FIT to qualifying applicants. Auctions with price bidding are also introduced for wind projects, which previously followed a business-to-business unsolicited bid

negotiated approach. Procurement using reference price or direct selection is distinct from auction selection, suggesting PLN flexibility in offering a fixed tariff or negotiating under a local production cost cap.

In selecting a developer, Regulation 12 requires PLN to carry out due diligence on the technical and financial capabilities of the candidates, adding little to prudent business practices presumably in place already. It also permits imposing fines and sanctions in the PPA in the event of completion delay caused by the project developer.

Regulation 12 also contains several provisions that may be considered attractive to renewable energy developers, as follows:

For solar and wind energy developers, Regulation 12 requires PLN to operate any solar or wind energy based plant with a capacity of up to 10 MW on a 'must run' basis, meaning that PLN must dispatch qualifying projects if they are available to produce energy.

Developers developing hydropower, biomass, biogas and geothermal projects will be permitted to negotiate with PLN on matters relating to the development of the transmission interconnection between the plants and PLN grid on a business-to-business basis. There may be increased flexibility for business-to-business negotiation on transmission matters.

PLN is required to standardize its procurement process and the final form of PPA that will be entered into by it and a renewable energy developer.

It is unclear whether Regulation 12 would help Indonesia reach its target of 23% of renewable energy share in the national energy mix by 2025. Currently, the renewable energy share in the national energy mix is far below the target at only 5%. This low current figure is unfortunate considering Indonesia's renewable energy potential .

A number of policy analysts suggest that the Government should not be content with Regulation 12, as profitability and bankability under the new FITs are questionable. Some warn against too much reliance on PLN to develop renewable energy and would encourage more efforts to entice private entities to participate in the renewable energy sector. Suggestions include making it easier for renewable energy developers to obtain financing in the country and simplifying the process for the developers to obtain licenses for the projects. Currently, the licensing process still includes applications to various agencies (especially at regional government level), which involves risks of delays. Having one authority (for example, the Investment Coordinating Board or BKPM) issue various licenses might help build investors' confidence in investing in the country's renewable energy sector.

1. The tariff for geothermal and waste-to-energy may be equal (i.e. 100% of the local production cost), if the local production cost is higher than the national average production cost. If the local production cost is the same or lower than the national average production cost, the tariff will be determined based on mutual agreement between PLN and the developer↩

2. If a renewable energy developer is appointed through direct selection, the tariff will be determined during the direct selection process.↩

3. Reference price means the applicable caps under Regulation 12 but it is not clear on whether the method is essentially similar to direct selection, but with the use of reference price.↩

4. Direct selection is not specifically elaborated in Regulation 12. However, some government regulations governing the power sector defined direct selection as a selection method by comparing proposals from a minimum of two candidates.↩