



8 September 2014

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By email: [DSD.REESReview@sa.gov.au](mailto:DSD.REESReview@sa.gov.au)

Dear Mr Denlay

### **RE: REES CONSULTATION PAPER AUGUST 2014**

ERM Business Energy welcomes the opportunity to respond to the Department of State Development's (DSD) *REES Consultation Paper* (the Paper).

#### **About ERM Business Energy**

ERM Business Energy (ERM Power Retail Pty Ltd) is a subsidiary of ERM Power Limited, an ASX-listed company with interests in electricity sales and generation, and gas production and exploration across Australia. Since launching in 2007, ERM Business Energy has grown to become the fourth largest electricity retailer, by load, in the National Electricity Market, and the only energy company licenced to sell electricity in every state and mainland territory. As a specialist business-only energy retailer, we have secured over 16%<sup>1</sup> market share of the large business market, with increasing success in the small business market.

As a business energy specialist, we are well placed to comment on the proposed expansion of the Residential Energy Efficiency Scheme (REES) to the business sector.

#### **A phased approach is required**

In our view, DSD's proposed framework misaligns the customers that are captured by scheme liability and the activities that they may undertake to benefit from the scheme. The DSD's proposed customer participation threshold of 30GWh means that the majority of large consumers would be included in the scheme; however, the primary contributors to their energy load cannot be addressed with the limited list of eligible activities proposed.

We understand that DSD is considering introduction of other energy saving methodologies over time that will facilitate a broader range of commercial energy efficiency projects. The Paper also indicates that DSD is exploring options for certificate trading to allow obliged retailers to procure energy savings from a greater range of sources. However both these initiatives will take time, and will not be implemented to support the REES expansion from 1 January 2015.

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<sup>1</sup> Based on market data as at March 2014.

We therefore propose a staged approach to expansion to the business sector. This approach would include small to medium businesses only (for example, those consuming up to 1GWh per annum) in the scheme from 1 January 2015. These businesses are generally well placed to benefit from the list of activities proposed in the Paper. At a later stage, coincident with the introduction of new commercial-focussed energy savings methodologies and certificate trading facilities, the participation threshold could be increased to include larger businesses.

ERM Business Energy believes this approach will be a more equitable outcome across all customers that will ultimately bare the cost of obliged retailers' liabilities.

Our submission explores DSD's proposed framework in the following structure:

1. What is a business customer?
2. What is a large business?
3. How can business customers save energy?
4. What is the role of activity trading in an expanded REES?
5. What is the most appropriate metric for energy savings?
6. ERM Business Energy's proposal

If you would like to discuss the content of this submission further, please contact me on the number below.

Yours sincerely,

[signed]

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## 1. What is a business customer?

The Consultation Paper proposes use of the customer definition as set out in the Electricity Industry Act 1996 for the purposes of determining inclusion in the REES. This definition reads:

*customer means a person who has a supply of electricity available from a transmission or distribution network for consumption by that person and includes—*

- a) the occupier for the time being of a place to which electricity is supplied; and*
- b) where the context requires, a person seeking an electricity supply; and*
- c) a person of a class declared by regulation to be customers;*

A place to which electricity is supplied is interpreted as an electricity connection point. While this is generally appropriate for describing small customers, it is not a suitable definition for larger business customers that often span a number of sites (or connection points). ERM Business Energy believes it would be more appropriate to define a customer with reference to a retail electricity contract.

In our experience, the majority of multi-site businesses choose to manage the business's energy matters centrally. This generally means there is one retail contract for all the business's sites, and bills for the individual sites may be sent directly to a corporate office. Those responsible for whole-of-business contract management have energy knowledge and expertise that is often not present at the individual sites. They are therefore best placed to understand the value of energy efficiency activities across the sites. Conversely, an individual site is unlikely to be able to weigh the costs and benefits of an energy efficiency activity if it does not have visibility of the site's electricity bills. We believe it is important that the definition of customer is aligned to the relevant decision-makers in a business.

ERM Business Energy recommends that this definition is extended to allow the aggregation of businesses sites under one retail electricity contract.

## 2. What is a large business?

The Paper describes the proposal as an expansion to the small to medium business sector. However it goes on to explain that to implement this focus, customers who consume 30GWh of energy per annum or more should be excluded from the scheme. ERM Business Energy believes this customer threshold goes beyond the target of small to medium businesses. Even if customers were defined by their aggregated annual energy contract as suggested above, we would certainly consider a customer that consumes close to 30GWh per annum a large business; their annual electricity bill is likely to be some millions of dollars.

To be clear, we do not oppose the concept of including large consumers in the REES. However we do not believe the proposed list of eligible activities could efficiently support energy savings at many of these customers' sites. Expansion of obliged retailers' liabilities to include sales to large customers without also providing reasonable options for large customers to benefit from the scheme would be an inequitable outcome.

## 3. How can business customers save energy?

Business customers are more likely to consider the economic benefits of energy savings than residential customers. This is particularly true for large business consumers. Given the significance of these businesses' annual energy costs, there is already a strong financial incentive to undertake energy efficiency improvements or operate from new high efficiency facilities. This is the case for many of our large customers. Many large energy consumers already have environmental or energy use policies that drive them to operate in an efficient manner.

Nonetheless, there remains opportunity for energy efficiency improvements in the business sector. The challenge for schemes such as REES is how to develop a robust regulatory framework that also provides the flexibility for businesses to undertake the energy efficiency improvements that are likely to deliver the greatest cost savings for their individual business. As REES provides a consumer-funded subsidy for improvements, it is important that the framework does not restrict the most cost-effective energy efficiency measures for participants.

ERM Business Energy is concerned that the proposed activities provide few opportunities for large business customers to benefit from the REES. Below we comment on each of the activities that DSD proposes to make available to business customers.

- *7.22 High efficiency appliances*

Although it is proposed that business consumers would be eligible for the purchase of high efficiency appliances under REES, the product requirements restrict many commercial applications and therefore the greatest potential for savings. For example, eligible refrigerators and freezers are limited to appliances with up to a 700 litre capacity. Cold storage required for food manufacturing or retail applications would not be eligible under this category. While a number of businesses could undertake this activity (for example, appliances in staff kitchens) the energy savings would generally be an immaterial proportion of their overall energy costs.

- *7.23 Remove and destroy an unwanted household refrigerator or freezer*

As above, this activity is restricted to “household style” appliances and therefore offers business customers little opportunity to benefit.

- *7.25 Aggregate Metered Baseline methodology*

As this methodology is particularly designed for activities where the energy savings are small on a site by site basis, this activity is not intended to offer material energy saving benefit to individual customers. The expected benefit for business customers is therefore unlikely to be deemed worth the effort required by the business.

- *7.26 Commercial lighting*

Of the business activities proposed, commercial lighting is expected to have greatest potential for business customers to benefit, with potential applications across all industries.

As we consider large energy consumers, we find that the primary contributors to their energy load tend to be specific to their particular business. For example, many large consumers owe much of their electricity bills to purpose-built heavy machinery, manufacturing equipment, air-conditioning systems and cold storage solutions. Energy savings associated with improving the efficiency of these items cannot be easily and accurately determined on a deemed basis, and therefore methodologies need to be developed that can allow a business to calculate or measure energy savings on a project basis. The NSW Energy Savings Scheme supports both a metered baseline and project impact assessment approaches which meet this need. If REES is to be expanded to include customers consuming up to 30GWh per annum, ERM Business Energy recommends that methodologies such as those utilised under the ESS are introduced to ensure large customers have reasonable opportunity to benefit from the scheme.

#### **4. What is the role of activity trading in an expanded REES?**

In our submission to the REES Review Directions Paper in August 2013, ERM Business Energy submitted our support for the expansion of the REES to the business sector on the condition that the scheme was

adjusted to a tradable certificate-based model. We appreciate the efforts of DSD in exploring the option to utilise other jurisdictions' certificate registries to enable certificate procurement towards REES obligations. We understand legislative changes are required to enable this change and that such changes will inevitably take time. However we are concerned that the significant scheme expansion proposed by DSD will be inefficient and costly without provisions for certificate trading.

ERM Business Energy maintains that there are significant competition and efficiency benefits that can be accessed by allowing obliged retailers to procure activities through a traded market. Key benefits of this approach include:

- Participation by a broader range of services providers – meaning greater range and quantum of activities being offered and customers that may be accessed.
- Price transparency provides competitive pressure to drive efficient costs.
- Clearer delineation of responsibilities between parties reduces duplication and increases accountability.

As scheme targets increase with the scope of the REES, it will become increasingly important that activities can be procured at competitive prices and delivered efficiently as the scheme expands. Conversely, the opportunity cost of failing to implement trading provisions as the scheme expands is likely to be material.

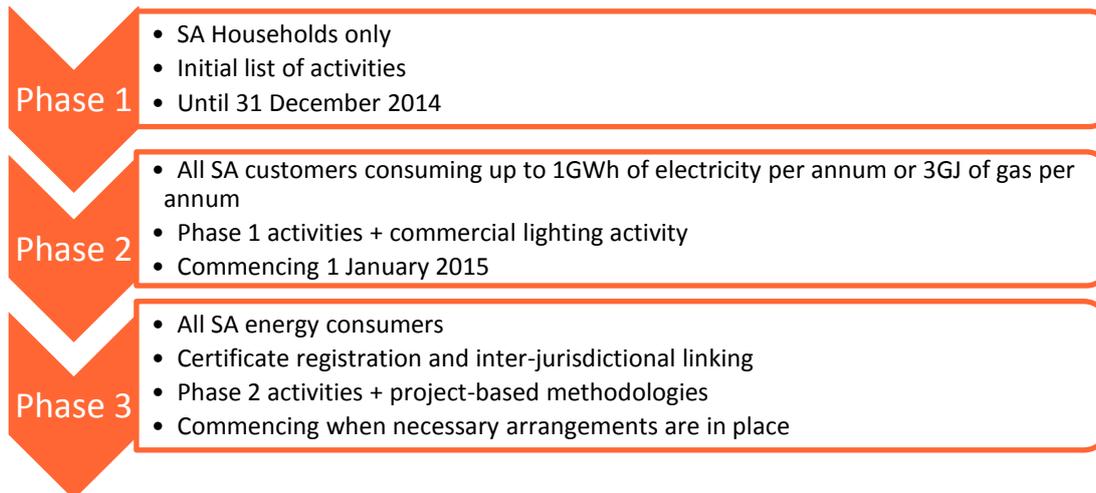
## **5. What is the most appropriate metric for energy savings?**

The DSD proposes an energy-based metric to measure energy savings. While we understand that this aligns with the amended scheme objective, it moves REES further from the approach of other jurisdictional schemes. All other jurisdictions use a carbon abatement metric (tonnes CO<sub>2</sub>-e) to measure energy efficiency improvements. DSD has indicated its preference to facilitate scheme linkage in the near future. If an energy-based metric was instated, conversion factors would be required to translate carbon abatement into energy savings and vice-versa. Conversion factors would likely need to vary for each jurisdiction as the carbon intensity varies. We suggest this is an unnecessary diversion from established norms that will serve little benefit while increasing complexity for participants and scheme administration.

We believe therefore believe that the existing carbon abatement metric should be retained.

## **6. ERM Business Energy's proposal**

ERM Business Energy recommends a phased approach to the expansion of REES to the business sector as outlined in the figure below.



If the operation of the scheme up until 31 December 2014 is labelled Phase 1, we propose that Phase 2 (commencing 1 January 2015) would expand the scheme to all SA customers consuming up to 1GWh of electricity or 3GJ of gas per annum. These customers will be well placed to participate in and benefit from the list of eligible activities proposed in the Paper because the likely savings from these activities will represent a larger proportion of the energy bill compared to larger users.

We propose that during Phase 1, DSD explore other energy saving methodologies that will allow large consumers to gain REES recognition for energy savings projects that cannot be measured on a deemed basis. The metered baseline and project impact methodologies offered under the NSW Energy Savings Scheme would be a helpful starting point.

Continued progress on inter-jurisdictional linking will also be required during this time. Close consultation with industry will be required to ensure an efficient and practical framework for activity (or certificate) registration and transfer of these between jurisdictions. Once this framework is developed, the necessary legislative changes can proceed.

The introduction of new energy saving calculation methodologies and trading facilities should be introduced in Phase 3. This Phase would also be an appropriate time to expand the scheme to include large energy consumers (those consuming more than 1GWh of electricity or 3GJ of gas per annum). Business Energy strongly recommends that the commencement date for Phase 3 is not set until there is certainty around the passage of legislation required for inter-jurisdictional linking, and new calculation methodologies have been finalised.