ACT Government
Environment, Planning and Sustainable Development

Energy Efficiency Improvement Scheme

Setting Key Scheme Parameters for 2022 by Disallowable Instruments:

Energy Efficiency (Cost of Living) Improvement (Energy Savings Target) Determination 2021 – DI2021-162

Energy Efficiency (Cost of Living) Improvement (Energy Savings Contribution) Determination 2021 – DI2021-163

Energy Efficiency (Cost of Living) Improvement (Penalties for Noncompliance) Determination 2021 – DI2021-164

Regulatory Impact Statement

Prepared in accordance with Chapter 5 of the *Legislation Act 2001*

June 2021

Contents

1. Executive summary

The *Energy Efficiency (Cost of Living) Improvement Act 2012* (the Act) establishes the Australian Capital Territory's (ACT's) Energy Efficiency Improvement Scheme (EEIS/the 'Scheme'), which aims to encourage the efficient use of energy; reduce greenhouse gas emissions associated with energy use in the Territory; reduce household and business energy use and costs; and increase opportunities for priority households to reduce energy use and costs. The EEIS establishes a Territory-wide Energy Savings Target (EST), defined as a proportion of a retailer's total electricity sales in the ACT.

The Act requires individual electricity retailers to achieve energy savings by delivering eligible activities to households and small-to-medium businesses. Eligible activities are determined by the Minister and include insulation, draught seals, efficient space heating and cooling systems, water heaters and other items that reduce energy bills and provide energy savings while maintaining quality of life. Whereas 'Tier 1' retailers (currently only ActewAGL Retail) must deliver energy savings activities, smaller, 'Tier 2' retailers can either deliver eligible activities or pay an Energy Savings Contribution (ESC). Any retailer that fails to meet its obligations under the Scheme within a given compliance period is required to pay a 'Shortfall Penalty'.

This Regulatory Impact Statement (RIS) was prepared in accordance with Part 5.2 of the *Legislation Act 2001*. The specific proposal considered in this document is for the following Scheme parameters to be set by the Minister for Water, Energy and Emissions Reduction in disallowable instruments for the 2022 compliance period:

- Energy Savings Target at 12.5%
- Energy Savings Contribution at $32/MWh, and
- Shortfall Penalty at $83/MWh.

These parameters are set by the following disallowable instruments:

- *Energy Efficiency (Cost of Living) Improvement (Energy Savings Target) Determination 2021*
- *Energy Efficiency (Cost of Living) Improvement (Energy Savings Contribution) Determination 2021*
- *Energy Efficiency (Cost of Living) Improvement (Penalties for Noncompliance) Determination 2021*

2. The authorising law

The EEIS is the ACT's market-based Energy Efficiency Obligation (EEO) scheme established under the *Energy Efficiency (Cost of Living) Improvement Act 2012* (the Act). The Act was passed by the Legislative Assembly on 3 May 2012 and the Scheme is currently legislated to run until 31 December 2030. Under the Act, a Territory-wide Energy Savings Target (EST) is

established, which determines the total energy savings to be achieved by individual retailers in a compliance period, expressed as a percentage of their total electricity sales in the ACT. A Retailer's Energy Savings Obligation (RESO) for a compliance period is calculated as follows: EST (%) x Electricity Sales (in megawatt hours or MWh). Those Tier 2 retailers that choose not to deliver energy savings activities are required to achieve their RESO through the payment of an Energy Savings Contribution (ESC). In cases where a retailer fails to meet their RESO, a Shortfall Penalty applies.

The specific level of each of these parameters may be set for several years in advance and reviewed and adjusted as needed. The EST must be determined by the Minister for Water, Energy and Emissions Reductions no later than six months before the commencement of the compliance period (by 30 June) if it increases; or no later than three months before the commencement of the compliance period (by 30 September) if there is no increase.

3. Policy objectives of the disallowable instruments

The three disallowable instruments set key parameters for the EEIS. The Objects of the Scheme, as set out in Section 6 of the Act, are to:

(a) encourage the efficient use of energy; and
(b) reduce greenhouse gas emissions associated with energy use in the Territory; and
(c) reduce household and business energy use and costs; and
(d) increase opportunities for priority households to reduce energy use and costs[1].

These Objects also deliver on key objectives of the *ACT Climate Strategy 2019–2025*[2] including: achieving net zero emissions in the ACT by 2045 at the latest; building resilience to climate change impacts; and supporting a just transition to net zero emissions. As one of the most cost-effective ways for the ACT to reduce emissions and energy bills and, to date, the only legislated instrument for doing so, the EEIS is a key delivery mechanism of the Climate Change Strategy. The EEIS specifically supports the objective of a just transition through the Priority Household Target, by which a proportion of savings are delivered to priority households. The Objects of the Scheme further align with the current 10th Labor – Greens Parliamentary Agreement[3], the first action under which is to 'phase out fossil-fuel-gas in the ACT by 2045 at the latest, support energy grid stability and support vulnerable households'.

[1] Note that Object (d) is addressed through a separate disallowable instrument (*Energy Efficiency (Cost of Living) Improvement (Priority Household Target) Determination 2021* and regulatory impact statement.
[2] Source: https://www.environment.act.gov.au/__data/assets/pdf_file/0003/1414641/ACT-Climate-Change-Strategy-2019-2025.pdf/_recache
[3] Source: https://www.cmtedd.act.gov.au/__data/assets/pdf_file/0003/1654077/Parliamentary-Agreement-for-the-10th-Legislative-Assembly.pdf

4. Achieving the policy objectives

An independent review of the EEIS was completed in 2018 by Point Advisory[4] (the Review). The Review confirmed that the EEIS had fulfilled its four Objects and has been effective in reaching a large proportion of ACT households and businesses. Moreover, it has been efficiently delivered, with a positive benefit cost ratio of 4:1 and a majority of participants reporting bill savings[5].

Over the lifetime of the Scheme, more than 1.35 million energy saving items have been installed. These have delivered more than 7 million gigajoules (GJ) of lifetime energy savings, over $445 million of lifetime energy bill savings and lifetime greenhouse gas emission reductions of around 580,000 tonnes (tCO2–e). This is equivalent to taking approximately 190,000 cars off Canberra roads for a year. Since 2013, almost 78,000 households and businesses have participated in and benefited from the Scheme, including more than 20,500 priority households. Over 45% of ACT households have participated in the Scheme and are saving an average of $5.80 per week[6].

Updating the parameters for 2022 will enable continued achievement of the Objects of the EEIS.

5. Considering a level of ambition

Based on analysis conducted by Energetics, this section outlines the key Scheme parameters that have been identified through modelling as the ideal for maximising EEIS benefits in 2022.

It is important to note that prior to 2020, the EEIS determined energy savings in the ACT using a greenhouse gas emissions abatement metric. As of 2020, the ACT secured a 100% renewable electricity supply and, in line with this, the EEIS transitioned to an energy savings metric. This has implications for the Scheme settings because the numerical abatement values under the former abatement metric do not equate directly to the values under the energy savings metric. Given some ongoing uncertainty about the effect of the shift to an energy metric, the Scheme parameters were last set for 2021 and are again being set for just one compliance period in 2022. The targets may need to be adjusted further in future years to more precisely account for the effect of transitioning to an energy metric as more data becomes available.

[4] Source: http://www.pointadvisory.com/
[5] Source: https://www.environment.act.gov.au/__data/assets/pdf_file/0020/1221527/EEIS-Review-Part-1-Executive-Summary-ACCESSIBLE.pdf
[6] As per the 2019-20 Environment, Planning and Sustainable Development Directorate Annual Report, available at https://www.planning.act.gov.au/about-us/annual-reports

5.1 Setting the Energy Savings Target

The EST setting aims to optimise EEIS outcomes which are measured in energy savings, bill savings and Net Present Value (NPV) to the ACT economy.

It is recommended that the EST be increased to 12.5% for the 2022 compliance period. This is supported by detailed analysis, as outlined below.

The EST has been set at 8.6% for the previous six compliance periods from 1 January 2016 to 31 December 2021. The 2018 Review into the EEIS recommended that the ACT Government continue the Scheme at the existing level of ambition (energy savings equivalent to 8.6% of electricity sales) and with a pass-through cost of $4/MWh. This was partly on the basis that there was some uncertainty introduced into the modelling through changes to eligible activities (namely the removal of low-cost lighting measures, which had featured prominently in the early years of the Scheme's operation). However, analysis of available information about the operation of the Scheme in 2021 suggests that the pass-through cost of $4/MWh is too high for the current level of ambition. As such, the modelling suggests that an increased EST can be achieved without requiring an increase in the pass-through cost.

Amendments to the Act relating to the adoption of an energy metric in place of an abatement metric commenced on 1 January 2021. The greenhouse gas emissions metric was changed to an energy metric because the ACT's 100% renewable electricity supply would otherwise effectively exclude any electricity saving activities from being delivered by the EEIS. The changes removed the definition of an emissions multiplier from the Act's dictionary and from all relevant equations and sections, replacing it with the energy measure of megawatt-hours (MWh). As noted above, the numerical abatement values under the former emissions abatement metric do not equate directly to those under the energy savings metric, which consequently affects target setting in order to maintain an appropriate level of ambition for the Scheme. To maintain the effectiveness of the Scheme under an energy metric, an increase in the EST is necessary and, as noted above, this is feasible without increasing the cost of the Scheme to consumers. The data will continue to be monitored in the coming years to assess the ongoing effect of the transition, and whether a further increase is warranted.

In addition to ensuring that the EEIS continues to deliver on its key objectives, an increased EST will further incentivise the delivery of a range of cost-efficient energy savings measures in the ACT. When the Scheme extension was modelled in 2018, it was assumed that the bulk of energy savings activities being delivered in future years would be home insulation measures as these were thought to be the lowest cost source of energy savings. While eligible, insulation activities have not yet been delivered under the Scheme due to the absence of a ready pool of certified installers in the ACT. Insulation training has now commenced that will enable delivery of insulation activities in accordance with the *Energy Efficiency (Cost of Living) Improvement (Eligible Activities) Code of Practice 2020 (No 2)*. This

will create a new cost-efficient pathway in 2022–23 for the Tier 1 retailer to meet its obligations under the Scheme.

5.2 Pass-through costs

This section describes processes for estimating the pass-through costs and how those will translate into key Scheme parameters.

The EEIS is funded via pass-through costs incorporated in the electricity bills of all ACT energy users. ActewAGL Retail is the only Tier 1 retailer, and the only retailer that is currently delivering activities. ActewAGL Retail is also a regulated retailer, meaning that its EEIS pass-through costs are determined by the Independent Competition and Regulatory Commission (ICRC)[7]. This determination is made annually, based on a methodology that takes account of legislative requirements and cost estimates provided by ActewAGL, and is "subjected to a forward-looking prudency and efficiency assessment by the Commission"[8]. For 2019–2020, this review resulted in an approved pass-through cost of $115.93/tCO$_2$e, or $4/MWh[9]. This means ActewAGL Retail is permitted to pass through up to $4/MWh to deliver EEIS activities at the level of the current EST of 8.6% of retail sales.

The recommendation based on Energetics' analysis is that the existing pass-through cost of $4/MWh be retained for the 2022 compliance period.

5.3 Setting the Energy Savings Contribution

Smaller Tier 2 retailers are able to pay an Energy Savings Contribution (ESC) to meet their obligation under the EEIS. This is in recognition of the increased difficulty for smaller retailers to deliver energy savings in the ACT. A Tier 2 retailer's target is calculated in the same way as a Tier 1 retailer target. All Tier 2 retailers currently opt to pay the ESC as an alternative to delivering activities. The ESC is currently set at $46.50/MWh by way of the *Energy Efficiency (Cost of Living) Improvement (Energy Savings Contribution) Determination 2020 (No 1)*.

It is recommended that the ESC be reduced to $32/MWh. This is based on the recommended change in the EST. The ESC calculation is based on the expected average cost of compliance for a Tier 1 electricity retailer. This figure will continue to be monitored and adjusted based on the actual costs determined by the ACT's Independent Competition and Regulatory Commission.

[7] Source: https://www.icrc.act.gov.au/energy/electricity
[8] ICRC, 2019. *Electricity Model and Methodology Review 2018-19*, available at https://www.icrc.act.gov.au/__data/assets/pdf_file/0011/1369190/Report-5-of-2019-Electricity-Model-and-Methodology-Review-Final-Report.pdf, pp.33-34.
[9] ICRC, 2019. *Final decision: Retail electricity price recalibration 2019-20.* Available at https://www.icrc.act.gov.au/__data/assets/pdf_file/0003/1372773/Report-6-of-2019-Electricity-Price-Reset-2019-20.pdf. Pp. 28-29.

5.4 Setting Penalties for Noncompliance

The Shortfall Penalty acts as an upper limit to potential costs for delivering activities and aims to disincentivise non-compliance, including the risk of Tier 1 retailers not delivering activities. If a retailer's energy savings result is a net shortfall, the retailer is liable to pay a Shortfall Penalty to the Territory.

The Shortfall Penalty is currently set at $120 per MWh by way of the *Energy Efficiency (Cost of Living) Improvement (Penalties for Noncompliance) Determination 2020 (No 1)*. The ICRC uses the Shortfall Penalty as a ceiling on its price determination. Compliance has been extremely high, and the Shortfall Penalty has never been applied.

The proposed Shortfall Penalty of $83/MWh is commensurate with the other proposed settings, being 2.6 times the value of the ESC, as per current practice. This setting is recommended to be an incentive for retailers to deliver an energy savings result consistent with the set targets.

5.5 Summary of proposed key Scheme parameters

For the reasons outlined above, the EEIS settings for the 2022 compliance period are as follows:

- Energy Savings Target at 12.5%
- Energy Savings Contribution at $32/MWh, and
- Shortfall Penalty at $83/MWh.

As part of its analysis to inform the 2022 settings, Energetics modelled several alternative options for Scheme settings. This modelling shows that emissions abatement increases in line with a higher EST but that this also translates into higher pass-through costs to consumers. Moreover, when the EST is set above around 18%, the Scheme becomes a burden on the ACT economy. In contrast, a moderate increase in the target (for instance to 9.5%) maximises the net present value (NPV) of the Scheme. However, this would not address the reductions in emissions abatement that have followed the transition to an energy metric, thus curtailing the Scheme's ability to deliver on its legislated objectives.

The modelled option of increasing the level of ambition (to 12.5%) while maintaining the expected pass-through cost of $4/MWh, is considered optimal as it will result in a 15% decrease in natural gas emissions in 2030. Importantly, this outcome will be achieved without imposing additional costs on ACT electricity consumers and there will be only a minor impact on the value of the Scheme to the ACT economy.

A final option of not setting parameters at all would be inconsistent with the Act, as it would not provide retailers with the information they need to participate in the Scheme.

6. Strategy for further implementation, review and consultation

The regulatory reforms presented here will be achieved through a continuation of current EEIS implementation processes. The Act allows the EST and ESC to be reviewed and re-set by the Minister throughout the life of the Scheme. It is important to set key Scheme parameters with a long lead time to provide business certainty, which is why the Act requires that increased targets be set at least six months ahead of the relevant compliance period.

The ACT Government will continue reviewing Tier 1 delivery costs, pass-through costs and the energy savings outcomes, and adjust Scheme parameters if needed.

7. Complementarity

The determinations are not inconsistent with the policy objectives of another Territory law.

8. Human rights

The determinations do not engage any human right set out in the *Human Rights Act 2004*.

9. Assessment of the consistency of the proposed law with Scrutiny of Bills Committee principles

The Standing Committee on Justice and Community Safety (Legislative Scrutiny Role) must consider whether any instrument of a legislative nature made under an Act which is subject to disallowance and/or disapproval by the Assembly:

i. is in accord with the general objects of the Act under which it is made,
ii. unduly trespasses on rights previously established by law,
iii. makes rights, liberties and/or obligations unduly dependent upon non reviewable decisions, or
iv. contains matters which in the opinion of the Committee should properly be dealt with in an Act of the Legislative Assembly.

The position in relation to each term of reference is as follows.

(i) is in accord with the general objects of the Act under which it is made

As noted above, the proposed settings are in accordance with the general objects of the Act.

(ii) unduly trespasses on rights previously established by law

The proposed settings do not unduly trespass on rights previously established under law.

(iii) *makes rights, liberties and/or obligations unduly dependent upon non reviewable decisions*

The proposed settings do not make rights, liberties and/or obligations unduly dependent upon nonreviewable decisions.

(iv) *contains matter which in the opinion of the Committee should properly be dealt with in an Act of the Legislative Assembly*

The proposed settings do not require further amendments to an Act and the subject matter is appropriate for disallowable instruments.

10. Conclusion

This Regulatory Impact Statement was prepared in accordance with Part 5.2 of the *Legislation Act 2001*, to consider the following Scheme parameters for the EEIS for the 2022 compliance period:

- Energy Savings Target at 12.5%
- Energy Savings Contribution at $32/MWh, and
- Shortfall Penalty at $83/MWh.

These parameters are consistent with the objectives of the *Energy Efficiency (Cost of Living) Improvement Act 2012* and will adjust for the impacts of the transition to an energy metric, thereby ensuring that the Scheme remains fit-for-purpose.