



MAJOR ELECTRICITY
USERS' GROUP



Hon Gerry Brownlee
Minister of Energy
Parliament Buildings
WELLINGTON

Dear Mr Brownlee

Energy Efficiency and the Role of EECA

We are writing to ask you to review the sizeable level of government spending on the Energy Efficiency and Conservation Authority (EECA) and energy efficiency programmes. We see savings in this area as an obvious opportunity for the government to consider in the context of the Cabinet Expenditure Control Committee's work on the 2009 Budget.

The efficient use of energy vs energy efficiency

1. The government's prime economic goal is to lift standards of living in New Zealand by raising the rate of productivity growth. Energy is used efficiently when the value of the output produced by the last unit consumed is equal to the cost to society of forgoing the use of that last unit for some other purpose – the opportunity cost. The same efficiency condition is true for every other factor of production – labour, capital, raw materials and all intermediate goods. For maximum benefit all inputs should be used efficiently. It is inefficient to use less energy if it means using another scarce input, such as labour, more wastefully.
2. The alternative goal of 'energy efficiency' is incompatible with the efficient use of energy and therefore with the government's prime economic objective. In addition to the problem that it ignores the need to use all inputs efficiently, it also ignores the point that optimal energy usage will also depend on changes in the production mix in the economy. If more energy-intensive products can lift standards of living it is optimal to supply them, even if the nation's energy consumption per unit of GDP were to rise.¹
3. It follows that EECA should not be promoting 'energy efficiency'. It is a matter of public record that EECA has been unsuccessful in doing so in any case. The independent Situation Assessment Report reviewing the performance of EECA to achieve the goals of the first National Energy Efficiency and Conservation Strategy (NEECS)² reported³:

“Between 2001 and 2004 New Zealand's energy efficiency performance improved by around 0.4% p.a. – the average rate of improvement over the five years prior to the release of the Strategy (ie between 1996 and 2001) was around 0.75%.”

¹ Refer to the speech *Energy Efficiency* by Roger Kerr for a more detailed discussion of the confusion about energy efficiency at http://www.nzbr.org.nz/documents/speeches/speeches-2000/energy_eff.pdf

² The first NEECS commenced in 2001 and was replaced by the second NEECS in 2006.

³ Refer <http://www.eeca.govt.nz/eeca-library/eeca-reports/report/situation-assessment-report-neecs-06.pdf>, p9.

As so often happens with a failed government programme, the response of the previous government was to expand it.

The role and activities of EECA

- 4 EECA's last annual report states that its role is to promote sustainable energy by changing the way New Zealanders think about and use energy. It promotes "energy efficiency and renewable energy issues". This combination of woolly mantra and 'we know best' paternalism bears no obvious relationship to the efficient use of energy or the promotion of the government's prime economic goal. So how did this state of affairs come about?
- 5 In 2000 the Labour coalition government, as part of a political deal with the Green Party, supported the passage of legislation establishing EECA as a Crown entity with appropriations being administered by the Ministry for the Environment.⁴ Prior to 1 July 2000, core energy efficiency policy and EECA activities were administered by the Ministry of Economic Development (MED). Since EECA was established its role and funding has grown under the political patronage of the Greens.
- 6 EECA currently has 109 FTE staff, an annual operating budget of \$23 million and manages grants of \$30 million⁵. To put this into perspective, the Electricity Commission – which manages the important functions⁶ of managing and improving the rules of the electricity market, economic regulation of transmission investment approvals, transmission pricing and default transmission contracts – has 50 staff⁷ and an operating budget of approximately \$19 million⁸.
- 7 There are concrete grounds for concern about EECA's ability to oversee the spending of taxpayers' money. The EC reportedly refused to contract with EECA for the delivery of services in 2007/08 because it was not satisfied with the cost-benefit analysis justifying the use of levy monies accrued by the EC. The EC therefore only spent 46 percent (\$5.957 million) of its appropriation of \$13.074 million⁹. The EC, in consulting on draft appropriations for 2009/10, states: "The 2008/09 appropriation included a provisional allocation of \$5.000 million for EnergyWise programmes, subject to the provision of a business case meeting the Commission's criteria. A sustainable business case has not been able to be achieved and the Commission will not be purchasing EnergyWise programmes and will not be collecting funding for this in future."¹⁰
- 8 EECA has also become an important agent for implementing the *New Zealand Energy Strategy to 2050 – Powering Our Future: Towards a sustainable low emissions energy system* finalised in October 2007¹¹ (NZES). As the title of the NZES makes clear, energy policy under the previous administration was dominated by climate change policy and an obsession with renewable generation. The NZES gives little consideration to how energy policy might improve productivity and GDP. The October 2007 version of the NZES looks inconsistent with the priorities of the new government.

⁴ Refer Energy Efficiency and Conservation Act 2000, May 2000, http://www.legislation.govt.nz/act/public/2000/0014/latest/DLM54948.html?search=ts_act_Energy+Efficiency+and+Conservation+Act_resel&sr=1

⁵ Refer EECA, Briefing to the Incoming Minister, http://www.beehive.govt.nz/sites/all/files/Energy_Efficiency_and_Conservation_Authority_BIM.pdf, page 29

⁶ Note this memorandum does not consider the question of whether these functions or the current regulatory governance structure are optimal.

⁷ Refer David Caygill, EC Chair, speech to Energy Federation seminar, 17 December 2008.

⁸ Refer EC Annual Report 2007/08, pages 40 and 48. The EC operating budget excludes service provider contracts for market operations (\$29 million), managing the Whirinaki contract on behalf of the Crown (\$26 million) and electricity efficiency programmes (\$5 million). Web reference.

⁹ <http://www.electricitycommission.govt.nz/pdfs/publications/annual0708.pdf>
Ibid, p25

¹⁰ Refer EC consultation paper 'Proposed work priorities and appropriations for the 2009/10 financial year', 19 December 2008, paragraph 35 (b) (iii).

¹¹ <http://www.electricitycommission.govt.nz/pdfs/opdev/finance/Appropriations-0910.pdf>

Refer <http://www.med.govt.nz/upload/52164/nzes.pdf>

- 9 In short, the current focus and activities of EECA lack both an adequate public interest justification and clear objectives for which the Authority can be held accountable. Nor does the NZES appear to be aligned with the government's concern that New Zealand uses energy – and all other inputs – efficiently.

The potential role for the government in the use of energy

- 10 Aside from the misplaced goal of energy efficiency, other reasons are often cited for the government to intervene with specific measures relating to energy consumption. These include:
- a) Information asymmetry, eg the claim that the public has little expertise to gauge the relative efficiency of different appliances or vehicles;
 - b) Market prices do not include external costs such as possible climate change risks; and
 - c) Split incentives, eg the claim that owner-occupied households have different incentives to invest in energy-efficient equipment compared with owners of tenanted properties.
- 11 Different sectors of the economy will raise different policy issues and invoke a range of possible solutions. For example, in the transport sector, improving the efficiency of the vehicle fleet will be affected by a range of other government policies, from improving road infrastructure through to the global trend of vehicle manufacturers to improve average vehicle fuel efficiency. This requires a different understanding of policy responses compared with, for example, energy efficient practices and investment in the coolstore industry.
- 12 Some of the externalities, such as imputing a price into the economy for climate change risks, are better considered as part of more generic policy for the whole economy.
- 13 Other barriers, such as information asymmetry, can be managed by buyer research into expert opinions and by information provided by suppliers of competing products. Other options include voluntary codes of disclosure. New Zealand also has obligations to cooperate with Australia on changes in minimum performance standards for certain plant and equipment. Of course information is not knowledge. Forced disclosure may not help those who cannot interpret the information accurately.
- 14 The argument that private landlords will not invest optimally in their properties because tenants will systematically fail to assess them in relation to the cost of heating appears to be little more than a paternalistic assertion. Living standards and the quality of housing improved in New Zealand for many years without an EECA to 'change' people's behaviour. The rental value of landlords' properties is increased by a range of investments, including insulation and other energy-saving investments. Similarly, tenants value these benefits. People are not stupid, and while private arrangements are not perfect, government intervention in this area, having regard to its costs, is not obviously superior. There has also been speculation that EECA has crowded out private sector providers of energy efficiency advisory services.
- 15 There is also a question as to whether many of the grant schemes and other EECA programmes were established to deliver on Green Party political promises rather than being based on a robust economic cost-benefit rationale.
- 16 MED and other core departments such as the Ministry of Transport are responsible for energy efficiency policy in their particular sector. EECA in their Briefing to the Incoming Minister, under the Heading 'Focus on Delivery', starts with the statement "We are a delivery agency with a strong focus on action."¹² This raises a number of issues including:

¹² Refer EECA, Briefing to the incoming Minister, page 4.

- d) If EECA is the delivery agent, should not MED or other core departments have been responsible for cost-benefit analysis justifying programme expenditure?
 - e) Why does EECA have to be the delivery agent? Couldn't delivery functions be undertaken through a branch of MED or contracted out?
 - f) What is the purpose of the EECA board and is it needed? This appears to be a high-cost overhead for a delivery agency function.
- 17 In conclusion, current arrangements seem to reflect political patronage and anti-growth attitudes. They have never been supported by any rigorous public policy justification and are inimical to the achievement of the government's prime goal of achieving higher living standards through the more efficient use of energy and all other scarce inputs. We submit that EECA should be reviewed with a view to terminating activities that are inconsistent with the government's approach to energy and other policies. A rigorous review might conclude that EECA should be scaled back or wound up, with any residual activities being returned to MED or other departments.



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