

Triggering energy efficiency investments

A EURELECTRIC policy paper

September 2015

EURELECTRIC is the voice of the electricity industry in Europe.

We speak for more than 3,500 companies in power generation, distribution, and supply.

We Stand For:

Carbon-neutral electricity by 2050

We have committed to making Europe's electricity cleaner. To deliver, we need to make use of **all low-carbon technologies**: more renewables, but also clean coal and gas, and nuclear. Efficient electric technologies in **transport and buildings**, combined with the development of smart grids and a major push in **energy efficiency** play a key role in reducing fossil fuel consumption and making our electricity more sustainable.

Competitive electricity for our customers

We support well-functioning, distortion-free **energy and carbon markets as** the best way to produce electricity and reduce emissions cost-efficiently. Integrated EU-wide electricity and gas markets are also crucial to offer our customers the **full benefits of liberalisation**: they ensure the best use of generation resources, improve **security of supply**, allow full EU-wide competition, and increase **customer choice**.

Continent-wide electricity through a coherent European approach

Europe's energy and climate challenges can only be solved by **European – or even global – policies**, not incoherent national measures. Such policies should complement, not contradict each other: coherent and integrated approaches reduce costs. This will encourage **effective investment to** ensure a sustainable and reliable electricity supply for Europe's businesses and consumers.

EURELECTRIC. Electricity for Europe.

Triggering energy efficiency investments

A EURELECTRIC policy paper

September 2015

KEY MESSAGES

- Private energy efficiency investments remain lower than expected, often due to non-economic barriers;
- There is a clear need to revise the way in which investments in energy efficiency in the EU are being promoted through financing;
- The EU can play a vital role in sharing lessons learned and information on existing & innovative financing tools as well as standardising processes;
- Financing tools which leverage private investment and do not require refinancing via surcharges on the energy bill should be developed - including tools such as Energy Performance contracts (EPC), Energy Savings Agreements (ESA) or on-bill repayment.

Background

There is a universal understanding that energy efficiency is a key enabler for reaching the EU's climate and energy targets, as well as in the creation of a sustainable and secure future for Europe's energy system. The energy saving potential on the demand side, specifically in buildings and transport, has been largely recognised with policy measures aimed at reaping this potential already being implemented. The market for energy efficiency products and services is expanding in size and diversity, moving closer to the needs of customers across the EU.

In its recent studies of whether the EU is on track to achieving its energy efficiency target, European Commission estimations project a minor miss of around 1% (19% of the 20% target by 2020). This gap does not stem from a lack of available technologies or legislation, but to a fair extent from a lack of attractive solutions for efficiency investments. In this context, the market penetration of energy efficiency products, especially in buildings and transport, has proven to be a challenge, despite the fact that they often present economically beneficial solutions to customers. It is worth noting that these two sectors comprise almost 70% of the EU's total energy consumption. While today's energy efficiency market offers a range of products and services which allow for significant reduction in energy costs, while at the same time improving sustainability, investment levels remain lower than anticipated. This is partly due to the fact that energy efficiency markets are still in development with new actors entering the stage and new products and business models being developed. A major concern is that the necessary financing tools for spur those markets are insufficient.

Energy efficiency investments can not only lead to direct energy returns, but may also create additional value streams to private owners and asset operators. Furthermore, these investments can trigger significant benefits to the public related to lower emissions, increased employment and reduced dependence on foreign energy imports. Energy efficiency actions which integrate all of these benefits should therefore be prioritised. Attention must also be paid to the possible "rebound effects" associated with these actions. When considering the upstream dimension of the best suited financing tools, the objective is to select the most relevant and profitable energy efficiency investments and consequently improve the effectiveness of funding.

EURELECTRIC believes that utilities can play a strong and active role in establishing and expanding markets for energy efficiency. The potential through building renovation, heat pumps and more efficient appliances is significant, particularly in the residential sector, and the required technologies are readily available. Utilities are central players in unlocking this potential. New business models have allowed the further development of close customer relations. Power providers are changing their role and are becoming more geared towards becoming suppliers of more than just energy as a commodity, and the related expansion of know-how has brought new technologies into the market. Due to their proximity to customers, utilities can also act as information providers or, through innovative financing models, they can also play a role in the financial execution of energy efficiency projects.

Delivering on energy efficiency requires financial tools

In the further development of energy efficiency products and services, serious concerns related to the financing of Energy Efficiency are being faced by markets and stakeholders. This is due to market failures as well as a lack of, or incorrect, information on the benefits of energy efficiency. The scale of investment needed to meet the EU's 2020 energy efficiency target is estimated at around €100 billion per year. While the European Commission recognises the need to boost private energy efficiency investments through targeted use of public funds, there is a need to adjust existing financing options and to introduce new solutions. In several EU Member States energy savings obligations have led to increased investments in energy efficiency, however the costs for projects under such schemes has been socialised, usually via the electricity bill. This has had negative impacts on the affordability and transparency of electricity costs.

In its 2014 Communication on Energy Efficiency¹, the European Commission highlighted how financing (along with policy implementation) is one of the key sectors to be improved in order to release the EU's full energy efficiency potential. Promoting financing in energy efficiency can be achieved through a number of levers, some of which have become common practice (e.g. dedicated credit lines & risk sharing facilities), while others are being implemented in national or regional jurisdictions. EURELECTRIC supports this analysis and has developed a set of considerations which should be taken into account by policymakers:

Investment tools face obstacles

EU energy efficiency legislation has done a lot to drive and develop energy efficiency products and markets. Yet, despite this effort, investment remains below expectations to achieve the target. There is a clear need to revise the way in which investment in energy efficiency is being promoted through financing. The Energy Efficiency Directive identified regulatory and non-regulatory which prevent capital investment. The list of obstacles is complex and includes:

- ❖ Limited access to finance;
- ❖ Long payback times compared to other investments;
- ❖ Sustainable energy investments suffer from higher perceived credit risk;
- ❖ Competing priorities for property owners;
- ❖ Complexity of projects binding investors' in-house capabilities and resources.

¹ COM(2014) 520

EU tools exist but need fine-tuning

Much has already been done to increase investments especially from the private sector, mainly through measures aimed at reducing investor costs and risk. EU legislation points towards measures for Member States to increase availability and facilitate access to finance. Also, at the EU level, instruments and budgets have been deployed. Financing tools at the EU level consist mainly of grant financing (such as Horizon 2020, Intelligent Energy Europe, European Local Energy Assistance) or hybrid instruments (European Energy Efficiency Fund, Structural & Cohesion funds). However, several barriers also exist in respect of these EU tools and their ability to fulfil their potential. The following problems have been identified:

- ❖ Processes are often unclear or non-transparent;
- ❖ EU mechanisms are primarily targeted at large scale projects while small scale investments are also needed (e.g. at the residential level).

The Commission's Communication on Energy Efficiency and its accompanying Impact Assessment identify the key drivers to work upon. The Communication notes that *'reaching the level of energy-savings considered in this impact assessment will require significant additional investments which will have to be primarily private. Public money, including the European Structural and Investment funds will have to be used to leverage these private investments and the right regulatory framework will have to underpin them'*.

For those providing finance for energy efficiency investments, work will be required to clearly demonstrate the business case for investors and financiers. Experiences and lessons learned from the different approaches adopted by Member States will be especially of value in this regard. As regards the beneficiaries of energy efficiency financing, better and more comprehensive information is needed about the full benefits of energy efficiency. These benefits go beyond simple payback of investment or kilowatt-hours saved, but include improved quality of life or enhanced competitiveness for businesses.

Embracing emerging financial instruments

Expanding the diversity of financing options will help address the different market context of technology for each individual project. Across the EU, a number of Member States have implemented innovative financing models for energy efficiency projects, either on a national or regional scale, often with notable success. The significant advantage for innovative models lies in the fact that they do not rely on social refinancing through the energy bill. The Energy Efficiency Communication already mentioned the positive benefits of diversifying financing options as it calls for making *'wider use of innovative financing in the form of standardised investment products to support energy efficiency financing products'*. EURELECTRIC believes that exchanging information and best practises at the EU level will be beneficial in addressing the investment gap. Therefore, a mix of improved existing tools, together with a broader and more coordinated application of innovative financing instruments, is considered as being the best way forward.

Recommended EU Action

EURELECTRIC believes that the non-economic barriers in financing need to be addressed at the EU level. This will lower the costs to promote energy efficiency and reduce the policy costs which are added to the electricity bill. In the current market, a vast portion of the technologies and products are competitive and available. Overcoming market failures without relying on incentives will be critical for reaching EU goals and to achieve the target investment levels.

The tools which will enable this include:

- ❖ **Energy Performance Contracts (EPC) and Efficiency Services Agreements (ESA)** are financing mechanisms which are proven to work well as financing models. They allow contracting customers to be provided with the planning, financing and installation of energy efficiency measures (technology and/or refurbishment) without the need to take on debt. This has proven to be very beneficial also for publicly managed buildings, where it is often not an option to take on debt for such projects. EURELECTRIC is convinced that the potential of such mechanism is however much bigger. Market uptake can be significantly enhanced through standardising contracts in the early stages. As the market evolves and EPCs are more established, such standardisation can be phased out and left to the market. This is already being envisioned in the Energy Efficiency Directive but action is now required in this regard.
- ❖ **Financing instruments combined with information campaigns** are the most efficient way to activate private investment. The economic and environmental benefits of each project must be adequately measured and presented to the relevant decision makers. This also means making access to data both easier and cheaper.
- ❖ **Standardising processes in public financing** would help lower the burden for interested customers. Public financing institutions play a vital role in those sectors where private investments remain low due to market failures. They usually offer long-term financing which work towards desired policy goals. They do this while being unaffected by economic cycles which would otherwise slow investments. EURELECTRIC believes that public financing bodies are crucial and increased standardisation would yield even better results.
- ❖ **Sharing lessons learnt from on-bill-repayment²** – Among the leading practices emerging at the international level to promote building investments (e.g. California) such schemes take advantage of the relationships that already exist between utilities and their clients in the residential sector. On-bill financing has been implemented with mixed results in several EU Member States. Building on these experiences and overcoming weaknesses could in the future provide a good basis for on-bill schemes to become safe and more broadly available financing schemes for investments in the residential sector.

² A mechanism used to improve the creditworthiness (or seniority) of energy efficiency investments by requiring them to be repaid in the utility or tax bill and through the existing payment collection infrastructures of utilities or public authorities.

EURELECTRIC pursues in all its activities the application of the following sustainable development values:

Economic Development

▶ Growth, added-value, efficiency

Environmental Leadership

▶ Commitment, innovation, pro-activeness

Social Responsibility

▶ Transparency, ethics, accountability



Union of the Electricity Industry - EURELECTRIC aisbl
Boulevard de l'Impératrice, 66 - bte 2
B - 1000 Brussels • Belgium
Tel: + 32 2 515 10 00 • Fax: + 32 2 515 10 10
VAT: BE 0462 679 112 • www.eurelectric.org