

NEW ZEALAND BUSINESS ROUNDTABLE

SUBMISSION ON THE ENERGY EFFICIENCY BILL

OCTOBER 1998

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Summary

- The measures in the bill would reduce consumer choice and effective incomes. There is a cogent case that the burden will fall most heavily on low income households that are cash constrained.
- The analysis in this submission finds no obvious offsetting benefits, notwithstanding the bill's objectives of promoting greater energy efficiency, improved environmental outcomes and progress towards meeting New Zealand's international commitments on carbon dioxide emissions.
- The idea that consumer welfare must be improved if all users of energy are obliged to purchase more energy-efficient products overlooks the fact that consumers seek value for money rather than the most energy-efficient outcomes. Gaps between average energy efficiency and maximum technically achievable energy efficiency provide no basis for overriding consumer preferences.
- Nor is there any necessary relationship between greater energy efficiency and improved environmental outcomes. Furthermore, the case has yet to be made that mandatory energy efficiency measures are the most effective response to international pressure to reduce carbon dioxide emissions.
- The proposal to reinstate the minister's powers to limit domestic line or energy charges is unsound; any issues of market power should be addressed generically through the Commerce Act.
- We therefore submit that no adequate case has been made that this legislation is necessary or desirable. As it stands, the bill seems utterly inconsistent with the government's objectives of reducing government spending and regulatory burdens on businesses.
- In the New Zealand Business Roundtable's view, the bill should be rejected. We also consider there is no sound justification for the Energy Efficiency and Conservation Authority and for legislation and regulations relating to energy efficiency standards.

1 Introduction

1. This submission on the Energy Efficiency Bill (the bill) is made by the New Zealand Business Roundtable (NZBR), an organisation of chief executives of major New Zealand business firms. The purpose of the organisation is to

contribute to the development of sound public policies that reflect overall New Zealand interests.

2. The main features of the bill are summarised in the appendix to this submission. The explanatory notes to the bill assert that energy efficiency measures are the least-cost way that New Zealand can reduce carbon dioxide emissions.
3. The NZBR has contributed to the climate change debate in New Zealand in recent years through submissions on consultative documents and by bringing to New Zealand two eminent US climate change scientists. The NZBR also made a submission on 23 May 1996 opposing the proposed regulation of the energy efficiency of new buildings under clause H1 of the Building Act 1991.
4. This submission comments on the rationale for the proposed measures in the bill and their likely effects.

2 The rationale for mandating energy efficiency

1. The explanatory note to the bill argues that "[e]nergy efficiency provides both cost savings and environmental benefit by maintaining energy services while purchasing less energy and reducing environmental impact". It also asserts that "[m]any cost-effective opportunities to improve energy efficiency have been identified but for various reasons they are not adopted by the market".
2. This rationale is at once a counsel of perfection and an illusion. It is a counsel of perfection because, by the same logic, the state could argue that all human activity – eg child-rearing, family life, work practices and the use of leisure time – should be regulated since many individuals demonstrably depart from best practice, as determined by experts. It is an illusion because it presumes that the experts know what is best and that government regulation is invariably efficacious.
3. The bill fails to recognise that energy efficiency and environmental impact are only two of the many factors that individuals will take into account in making decisions. If the overall welfare of New Zealanders is the objective there is no basis for making these two factors paramount. To illustrate the trade-offs, lighter vehicles may use less fuel, but they may also be less safe. Similarly, the most energy-efficient buildings may be inconvenient in use and uncomfortably hot in summer. Furthermore, their greater capital cost may push up rents and force low income households to spend less on such basics as food, education, health care or home safety. Is it right for middle class voters to impose on the poor their views as to what constitutes value for money?
4. Nor can it be assumed that the bill's two goals are always complementary. It is easy to identify situations in which greater energy efficiency conflicts with environmental concerns. For example, it might be energy efficient to bulldoze a road directly through an environmentally sensitive area. Alternatively, the more fuel-efficient vehicle may be the noisiest.
5. In reality, the fact that many energy efficient opportunities are not taken up is exactly what we should expect to observe in any sound set of social

arrangements. Individuals can be expected to differ in the views they take about the trade-offs offered by energy-conserving products and devices. Unregulated producers will provide them with a choice that reflects available technologies and willingness to pay. No utility-maximising consumer will necessarily buy the product that is most energy-efficient in a technical sense. Nor will many consumers necessarily agree with expert views on what they should be assuming about future energy prices and technologies and their personal rate of discount.

6. Our 23 May 1996 submission considered other arguments for mandatory measures that relate to discrepancies between actual consumer behaviour and that deemed to be optimal by expert opinion or bureaucratic judgments. In all cases it pointed to reasons why governments should hesitate to override consumer choices. A copy of this submission is attached. We oppose the proposal in the bill to amend the Building Act 1991 to allow local authorities to require energy-efficient performance in new buildings for the reasons set out in this submission.

7. Finally, we note that clause 33 of the bill aims to reinstate the minister's powers to limit domestic line or energy charges. In our view this measure should be dropped. First, it is difficult to see any case for singling out electricity. The Commerce Act already contains generic powers to handle market power situations. Secondly, assertions of market power are commonly opportunistic because they are easy to make and difficult to rebut. Competitors and users have an obvious incentive to make loose and self-serving assertions about an incumbent's market power. Public policy analysts need to take a dispassionate, analytical approach. A recent Nobel laureate in economics, Gary Becker, has rejected assertions that industries like electricity and telecommunications can be described as natural monopolies. The magnitude of any entry barriers does not depend on current costs; it depends instead on how emerging technologies affect future costs. Finally, price control is likely to lead to cost-plus behaviour and undermine incentives to innovate, by perhaps eliminating the hope of a super-normal return. Alternatively, it may artificially reduce prices, lead to uneconomic consumption and be inconsistent with energy conservation. Open competition and unfettered innovation provide the most enduring solution to any problems of market power and have many positive conservation benefits as well.

3 The likely effects of the proposed measures

1. The proposed measures will reduce consumer welfare by restricting choice and reducing effective income. They limit consumer choice by denying consumers access to lower cost or better quality products that are less energy efficient. They will reduce effective consumer incomes by imposing opportunity costs in the form of:
 - the resources employed by the Authority;
 - the (deadweight) costs of the taxes imposed in order to fund the Authority;
 - the compliance costs that the associated regulations impose on suppliers;
 - the costs of the resources committed to lobbying the Authority and politicians by environmentalists, suppliers of energy-related products (such as suppliers of double-glazing and fibre-glass insulation) and users of energy-related products; and
 - the costs associated with bureaucratic politics as the Authority seeks to increase its power and access to resources in the face of competing claims by other bureaucracies.
1. All these costs will be experienced by households in the form of some combination of higher taxes, reduced government spending in other areas, higher product prices, lower wages or profits, and reduced choice.
2. A cogent case can be made that the burden of mandatory energy efficiency requirements would fall particularly heavily on low income households. This is because there is empirical evidence that these households behave as if they have much higher rates of discount than higher income, presumably less cash-constrained, households. Given the choice, capital-constrained households are likely to purchase cheaper houses or appliances at the expense of greater running costs or a shorter asset life than wealthier households.
3. There are no obvious benefits to set against the costs listed above. New Zealand, as a whole, does not have any air pollution or other environmental hazards that would obviously be best addressed by the proposed measures.
4. The only possible benefit identified by the explanatory note relates to carbon dioxide emissions. However, no case has yet been made in any official report that New Zealanders as a whole would be worse off as a result of projected global warming. Indeed, there might well

be economic benefits in respect of agricultural and horticultural production and trade. Many New Zealanders might prefer the warmer anticipated temperatures, in part through savings on heating fuel and possibly reduced winter-related illnesses, and judge that such benefits more than outweigh possible costs such as a greater incidence of summer-related illnesses.

5. Even if a case could be made that projected global warming would reduce New Zealanders' welfare, the proposed bill would still founder on the need to establish that its proposals represented a more cost effective remedy than other measures. Carbon taxes and tradable permits are amongst the possible alternative remedies.
6. Alternatively, the bill might reflect a view that New Zealand must be seen to be 'doing something' about carbon emissions as a result of international pressure. In this case, any measures New Zealand takes should be assessed in relation to the actions of other countries, such as Australia and the United States. The bill completely fails to reflect such a perspective.
7. The bill also imposes less tangible, but not necessarily less material, costs. These relate to the effect of the proposal on the rule of law. To impose a regulatory standard or control a price it appears that the Authority would effectively only require a ministerial signature and have to comply with process requirements that look far from onerous (see below). Under the bill, parliament appears to be delegating considerable regulatory powers to an agency that may be able to exercise those powers independently of parliament's detailed scrutiny. The uncertainties and reduced accountability undermine the certainty of property rights. This is a threat to innovation and investment.

3.9 One requirement is the duty to consult, but this does not oblige the Authority to respond to valid concerns. Another arguably inconsequential requirement is for the Authority to have regard to the costs and benefits of its recommendations. No mechanism is proposed for making this test objective, independent or meaningful. This is naïve. A future Authority could readily meet this requirement by postulating sufficiently long asset lives, high enough future energy prices and low enough consumer discount rates to warrant a conclusion that any households that were not better off as a result of its imposed standards were either irrational or ill-informed.

Appendix

Summary of the Main Features of the Bill

A.1 The explanatory note to the bill asserts that energy efficiency "offers the least-cost way to implement our commitment under the Framework Convention on Climate Change to reduce emissions of carbon dioxide". The bill aims to create "a framework for improving the energy efficiency of the New Zealand economy by establishing a statutory authority, a process for developing a national strategy, and the power to set performance standards".

A.2 The bill:

- provides, in Part 1, a statutory basis for the Energy Efficiency and Conservation Authority (the Authority);
- requires, in Part 2, the minister of energy to ensure that a national energy efficiency and conservation strategy is completed within 12 months of the Act coming into force and that a current strategy remains in force thereafter;
- provides, in Part 3, for the Authority to prepare "market transformation plans" to address "market failures" within any market or groups of markets as defined by the authority. These plans could include recommended performance standards and/or price controls for the minister of energy's approval;
- permits, in Part 4, the minister of energy, on the recommendation of the Authority, to make rules: prescribing energy performance standards; prescribing the labelling and packaging of energy-using products; requiring the provision of information concerning energy conservation in actual and proposed buildings; prescribing the form and manner of testing of energy-using products or buildings; requiring persons and firms to fill out forms relating to use of fuels, expenditures on research, development, acquisition, and operation of energy-using products and related technology; and providing for the control of the production, importation, distribution, sale, use, or disposal of energy-using products and the design, construction, and use of buildings. The bill would allow unlimited delegation of discretion of powers to the authority, subject to its compliance with some procedural matters set out in clauses 26(8) and 27. The Authority can determine that a rule should be imposed as a regulation under the Building Act 1991 or the Land Transport Act 1993.
- provides, in Part 5, for local authorities to require energy efficient performance in new buildings, amends the Electricity Act 1992 to reinstate the minister of energy's powers to control domestic line or energy charges in

respect of electricity, and amends the Land Transport Act 1993 so as to allow energy performance standards to be applied to land transport.