Contributor: Croatian Government Real estate Agency, in accordance with

Croatian Ministry of Physical Planning, Construction and State Asset

PROPOSAL FOR EnPC IN GENERAL BLOCK EXEMPTION REGULATION

PROPOSAL

In the proposed revision of the General Block Exemption Regulation we propose the following caption to be included:

Aid for the improvement of the energy efficiency of buildings may also relate to the facilitation of energy performance contracting in form of financial product or grants to the provider of energy savings via energy performance contract subject to following conditions:

For grant schemes all of the cumulative conditions must be met:

a) **Energy savings are delivered via investment of a private company as the investor. For the purpose of defining an investor status, agreement shall be compliant to assessment in line with EUROSTAT rules applied to accounting standards meaning that a private company assumes most of risks and rewards from the investment**
b) **Majority of investment (>50%) is in property intrinsically attached to a building not owned by the investor, and investment is carried out by an entity not connected to building owner**
c) **Agreement refers to renovation of an existing building (in use >3 years)**
d) **agreement is a long-term contract, with minimum 7 years of execution**
e) **grant scheme is conducted in a competitive manner, and competitive process is allocating significant value to reducing costs of the investment by reducing the aid level to minimum, whilst targeting achievement of highest level of energy efficiency after renovation**
f) **value of all energy savings delivered via energy performance contract are remunerated to provider of energy savings**
g) **grant aid is awarded after verified completion of all capital investment**

BACKGROUND OF ENERGY EFFICIENCY IN BUILDINGS POLICY

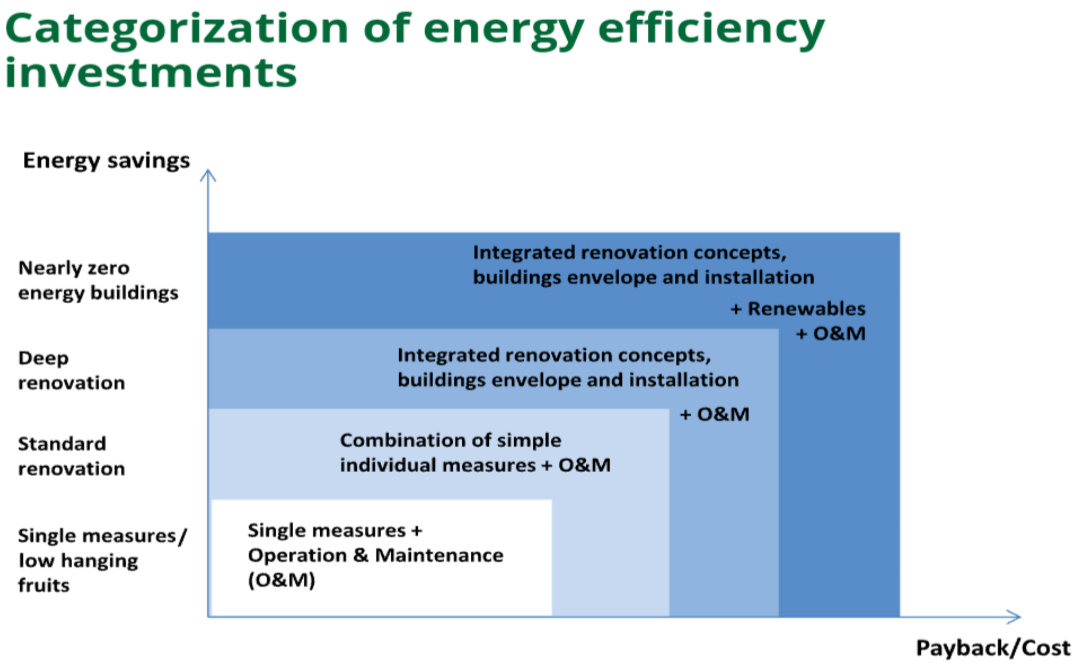
Buildings contribute to approximately 40% of energy consumption in EU. New regulation for newly constructed buildings ensure that energy consumption is reduced to a level which is well within environmental targets, particularly as reduced consumption enables supply of energy from renewable energy sources for majority of such energy consumption.

However, goals will not be achieved without renovation of existing buildings, which are less energy efficient.

Process of introducing energy efficiency in buildings is using government buildings to set an example and develop market for renovation of public buildings, from which effects are expected to spill over to private owned buildings, and EU has set ambitious mandatory goals for renovation of public buildings.

Public funds are not nearly sufficient to achieve energy efficiency targets in public buildings. To reach goals of renovation, basic outline is that private capital is to be mobilised in investment in renovation, and implementation of most efficient technologies must be encouraged to meet the targets and deep renovation of buildings is necessary.

Renovation intensity and aid



Source: European Commission (2014), "Technical Guidance on Financing the energy renovation of buildings with Cohesion policy funding", p. 46.

Without support, renovation will be focused on single measures/low hanging fruits, typically up to 30% energy savings. To achieve objectives, it is necessary that renovation exceeds 50% energy savings – deep renovation.

Mobilising private capital investment in energy efficiency in public buildings can be obtained only by deploying an Energy Performance Contract (EnPC), whereas the public institution – a building owner - contracts a private company to achieve energy savings in a public buildings as a service (Energy Service Company – ESCO).

Public procurement for EnPC

As public sector contracts are typically procured using public procurement method, typical Request for Proposals would include competitive bidding process, where ESCO's bid on criteria related to energy savings and costs, and an example can include following criteria:

Guaranteed savings (kWh)/year	Minimum savings ESCO undertakes to deliver – non delivery means no payments and the investment is at risk of ESCO	40%
Fee	Demanded fee which DOES NOT EXCEED VALUE OF GUARANTEED SAVINGS	40%
Other qualitative criteria		20%

ESCO performs renovation at its own costs, financing and organisation, and public building owner pays for energy savings ONLY UPON DELIVERY OF ENERGY SAVINGS.

This causes a specific relation where financial instruments, including guarantees, loans, equity and combination thereof are necessary, as ESCO invests into a building owned by the other contractual party, and it is without a doubt that developing specialised financial instruments will play an essential role in renovation of buildings using ESCO.

However, grants, blended with financial instruments are necessary to achieve any significant results.

In case where ESCO is contracted without support, in practice it means that renovation via EnPC arrangement will include mostly renovation for single measures/low hanging fruits. EnPC arrangement will in that case actually encumber reaching targets – measures are dimensioned to fit non-renovated building, and an ESCO does have rights of some kind of exploitation of such contract. This means that later renovation of a building envelope (walls, windows etc.) will cause damage to the ESCO, which makes it very difficult for public building owner to go into renovation due to legal issues.

EnPC and EUROSTAT statistical treatment

Criteria for private investment has been detailed by EUROSTAT in 2017 and 2018, and only in such case EnPC will be off balance sheet of the government. If an EnPC is not off balance sheet of the government, it would mean that a loan in kind was contracted. In this case, such arrangement is considered to be public costs (public debt), and budgetary limitations would apply. Aid to ESCO is in these instructions and guide published in May 2018. allowed without limitation ONLY if they are granted from EU sources.

For the case of providing aid to the ESCO, a condition must be met that ESCO is the investor. In such case, providing grant to public sector, weather through specialised fund or not does not solve the issue – if private capital is mobilised, ESCO is the investor and thus must be a grant (and financial instrument) beneficiary, assuming liabilities as it does in other cases of aid to private companies.

Competitive bid

In order to achieve deep renovation, public building owner can set up a competitive bidding process, whereas the market competition will force ESCO's to reduce demanded amount of a grant to a minimum level necessary, including accounting for available financial instruments. This can be achieved by simple attributing grant as price of a bid (Fee, as shown in a table), and grant is provided only for the amount exceeding fees collected on behalf of energy savings remunerations. Similar experience has been implemented in renewable energy sources, where market has reduced aid by implementation of competitive process.

In case of competitive bidding process, EU goals for public buildings can be met without distorting the market by simply setting minimum energy savings target in line with overall objectives. Similar model can be replicated for multiapartment buildings.

Unless support is sufficient to achieve deep renovation by mobilising private investment, objectives for energy efficiency will not be met.

PROPOSAL SUMMARY

Achieving ambitious goals in building renovation should focus on mobilisation of private capital in energy efficiency. Basic goal is that ESCO's are made able to invest in building renovation and that the investment is repaid for from energy savings upon their undisputed achievement. The proposal does not enable grant support for ESCO's private investment in providing energy efficiency investment in public buildings, and in extension in multiapartment buildings to be supported as energy service, as it is focused on financial instruments and intermediaries.

In case of energy efficiency in buildings, goals should focus on deep renovation, meaning that significant investment is made in building renovation, rather than investing in „low hanging fruits". In case of deep renovation, returns from have a spill over effect on overall renovation, whereas returns from implementation of investments with high returns are directed in higher investment in measures with longer period of returns.

In order to achieve ambitious goals set forth by EU, financial instruments will not be sufficient, and blending financial instruments and grants for private investors should not be disabled by imposing unnecessary restrictions. Currently, supporting private investment in public buildings, and essentially business of ESCO is restricted by article 38 of GBER.

For investment in public buildings not to be accounted as public debt, ESCO must assume most of risks and rewards of an Energy Performance Contract, and EUROSTAT has in 2017 and 2018 laid out a set of rules which define conditions under which this is possible. Meeting these criteria means that ESCO is an economical owner of the investment, even if legal ownership is with the building owner – in case of public buildings, a public unit, and in case of multiapartment buildings, co-owners represented by an association or another form of decision making.

A basic rule for an EPC to be accounted for off balance sheet of the government is that no liability of the public building owner occurs before energy savings are achieved and verified (or at least undisputed). This means that financial products such as factoring and forfaiting cannot be implemented to such level as to meet the need to support the ESCO's for deep renovation, as future savings cannot be subject to sale/purchase of receivables. To achieve ambitious goals, grant support to ESCO's should be enabled by changing article 38 of GBER.

We deem necessary for long term implementation of building strategies that GBER sets forth rules to ensure availability of grant support to ESCO's as beneficiaries, and we will provide a proposal to set the rules in a way which will ensure a fair market competition and enable grant support to mobilise private investment in energy efficiency in buildings.

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