Victoria Energy Upgrades Branch
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Victoria Energy Upgrades 2026-27 Targets

The Australian Energy Council ('AEC') welcomes the opportunity to make a submission to the Department of Energy, Environment, and Climate Action's consultation on *Victoria Energy Upgrades 2026-27 Targets Regulatory Impact Statement*.

The Australian Energy Council is the peak industry body for electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. AEC members generate and sell energy to over 10 million homes and businesses and are major investors in renewable energy generation. The AEC supports reaching net-zero by 2050 as well as a 55 per cent emissions reduction target by 2035 and is committed to delivering the energy transition for the benefit of consumers.

The AEC submits there is not enough evidence of significant new supply activity being created to support Option 2. For the reasons explained below, the AEC recommends Option 1 or Alt 1 or 2 to allow the market time to recalibrate while the Strategic Review is ongoing and place some much needed downward pressure on certificate prices. The Department could also consider setting a single interim target to provide retailers with some flexibility over the two-year period (e.g. setting a target of 8 or 9 million certificates to be met by the end of 2027).

Furthermore, the AEC recommends that the emissions factor be adjusted to be in trajectory with the National Greenhouse Accounts ('NGA') factors. There is a significant discrepancy between Victoria's 2024 electricity emissions factor of 0.77 and the proposal to freeze the emissions factor at 0.39, which the Department has acknowledged is not accurate. Because of this inaccuracy, using a 0.39 emissions factor lowers the actual emissions reductions impact of energy efficiency activity and increases compliance costs to meet the VEEC targets.

VEEC certificate costs continue to rise

The Victoria Energy Upgrades ('VEU') scheme is a major policy mechanism in Victoria for reducing greenhouse gas emissions through the provision of energy efficiency products and services. Unlike other jurisdictional schemes, the VEU scheme is designed around achieving emission reduction targets that increase each year. These targets are set years in advance, as are the methodologies that determine the emissions impact of different energy efficiency activities.

Historically, the VEU's legislated energy efficiency certificate targets (known as 'VEECs') were met through installation of simple and low-cost upgrades, mainly residential and commercial lighting. Many of these low-cost activities have since reached maturity and/or been phased out and have not been adequately replaced by new supply activity to meet the growing VEEC targets.

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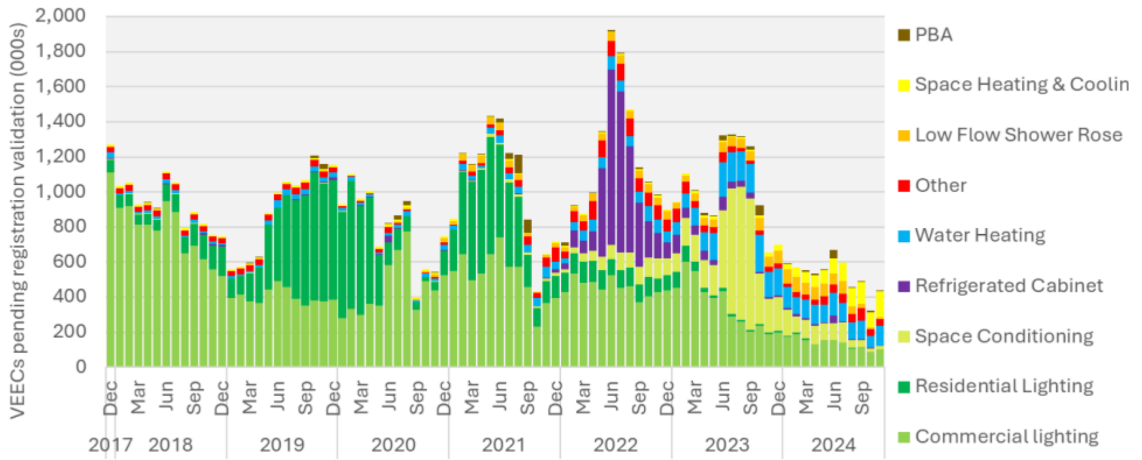
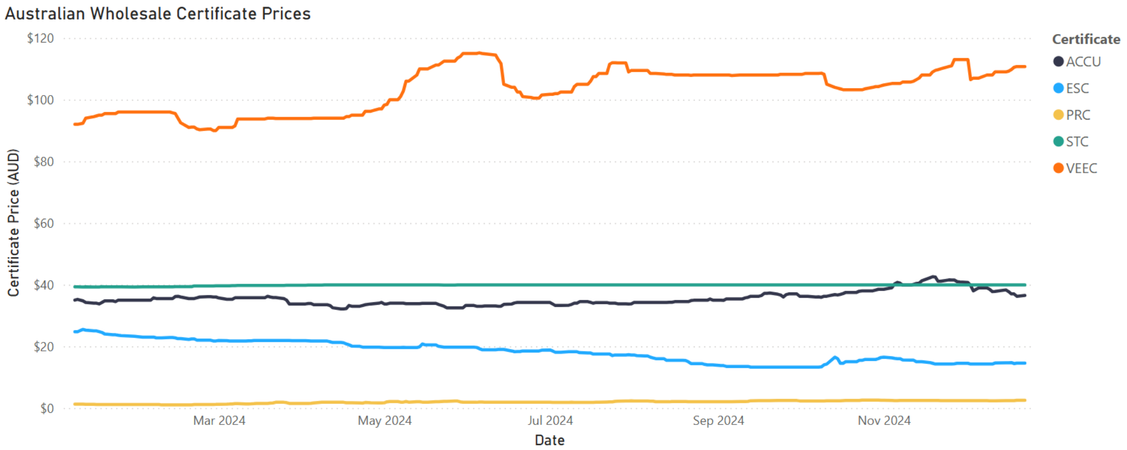
Figure 1: VEEC registration by activity type



Source: Green Energy Markets, November 2024 VEEC Snapshot

This has resulted in an ongoing imbalance between activity supply and prescribed demand, which is having perverse and negative impacts on certificate prices in Victoria. The figure below illustrates that Victoria has the highest certificate scheme prices compared to other similar jurisdictional schemes in Australia.

Figure 2: Wholesale Certificate Prices



Source: Northmore Gordon (prices as of 8 January 2025)

These high certificate costs flow into residential customer electricity bills, with the average residential customer paying about $52 to subsidise the VEU Scheme.[1] These costs are spread across all residential customers meaning that even customers that do not receive energy efficiency upgrades, which are disproportionately low-income customers, are paying.

The Department has acknowledged these affordability and equity pressures, and a Strategic Review is currently underway to improve the VEU scheme, which the AEC is part of. While the AEC has confidence in the direction of this Review, it will be some time until its recommendations are finalised and implemented.

[1] The 2024-25 Victorian Default Offer sets the retail cost of compliance with the VEU program as $13.26 per MWh. The average residential customer uses about 4MWh per year.

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High certificate prices likely to persist under Option 2

While Option 2 does propose lower VEEC demand targets compared to 2025, current market forecasts do not support the Department's view that enough new supply activity will be created on time to not only meet the targets but also saturate the market to lower certificate prices.

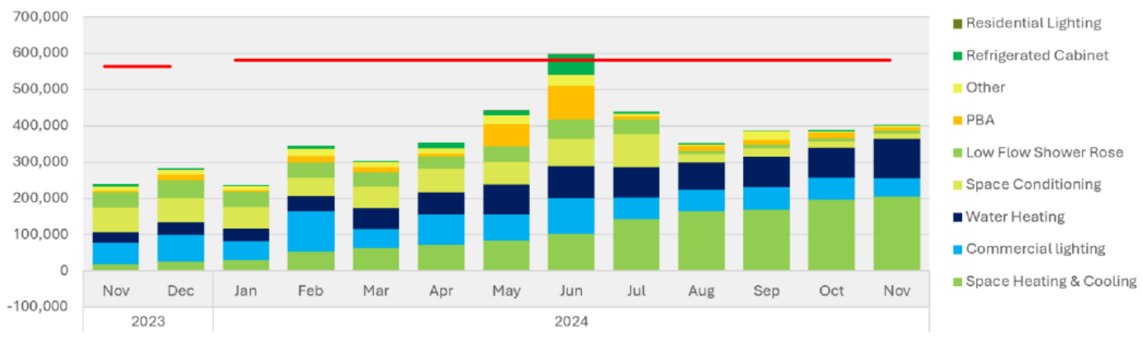
The figure below illustrates that the VEEC certificate surplus is declining quickly over time and is forecasted to be exhausted by the end of 2025.

Figure 3: VEEC Surplus and Forecast

Source: Green Energy Markets, November 2024 VEEC Snapshot

The exhaustion of this surplus is driven by new supply activity being significantly below the VEEC demand targets. The figure below, for example, shows new VEEC supply activity hovering at around 400,000 new certificates per month. This is well below the average monthly supply needed to meet the 2024 target (7.1 million), 2025 target (7.3 million), and even the proposed Option 2 target for 2026 (5 million).

Figure 4: Monthly Net Creation by Activity



Source: Green Energy Markets, November 2024 VEEC Snapshot

Given these market forecasts, high certificate prices are likely to persist under Option 2, which will place further cost-of-living strain on electricity bills.

The AEC strongly encourages pursuing Option 1 or Alt 1 or 2 to allow the VEEC market time to recalibrate while the Strategic Review is ongoing, which should contribute to lower certificate prices. In the event that new supply activity was to materially increase during the interim period,

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it just means there will be more surplus and liquidity for market participants (and the Strategic Review) to work with going forward.

The Department could alternatively consider setting a single interim target over the two-year period (e.g. setting a target of 8 or 9 million certificates to be met by the end of 2027) to provide both liable entities and the ESC with some flexibility in registering and surrendering VEECs.

Emissions factors should be adjusted in line with NGA

The AEC encourages the Department to reconsider the proposal to fix the electricity emissions factor at 0.39 for both 2026 and 2027. This factor is based on forecasts from 2019 that have not proven accurate, which the Department has acknowledged.

Table 1: Forecasted emissions factor vs actual emissions factor (based on NGA)

	2021	2022	2023	2024	2025
Forecast	0.95	0.81	0.67	0.53	0.39
Actual	0.96	0.85	0.79	0.77	?

Source: National Greenhouse Accounts factors

While the AEC understands the 2025 factor has already been determined, we consider that the discrepancy between the current factor of 0.77 and the forecasted factor of 0.39 is too significant for it to be re-used in 2026 and 2027. Using a 0.39 factor will misrepresent to customers the actual abatement value of their energy efficiency activity (reducing greenhouse gas emissions is a reason for purchase among some customers), as well as increase compliance costs because it means more certificates must be surrendered to meet the VEEC targets.

The AEC submits that an interim emissions factor be developed and enforced for 2026 and 2027 that is reasonably consistent with the trajectory of the actual Victorian emissions factor. This should not be overly complex to do given there are now existing methodologies and data available, both within DEECA, but also AEMO and the Clean Energy Regulator.

Comment on fee increases

The AEC notes that reduced emissions targets are translating into higher proposed fees, which will mean increased costs for liable entities to absorb. The AEC suggests this could be better done through the Victorian budget and/or should be left to the Strategic Review to consider as part of the long-term design of the VEU scheme.

Irrespective, any increase in fees will set an expectation among scheme participants for improved operational performance of the scheme.

Any questions about this submission should be addressed to Rhys Thomas, by email Rhys.Thomas@energycouncil.com.au or mobile on 0450 150 794.

Yours sincerely,

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