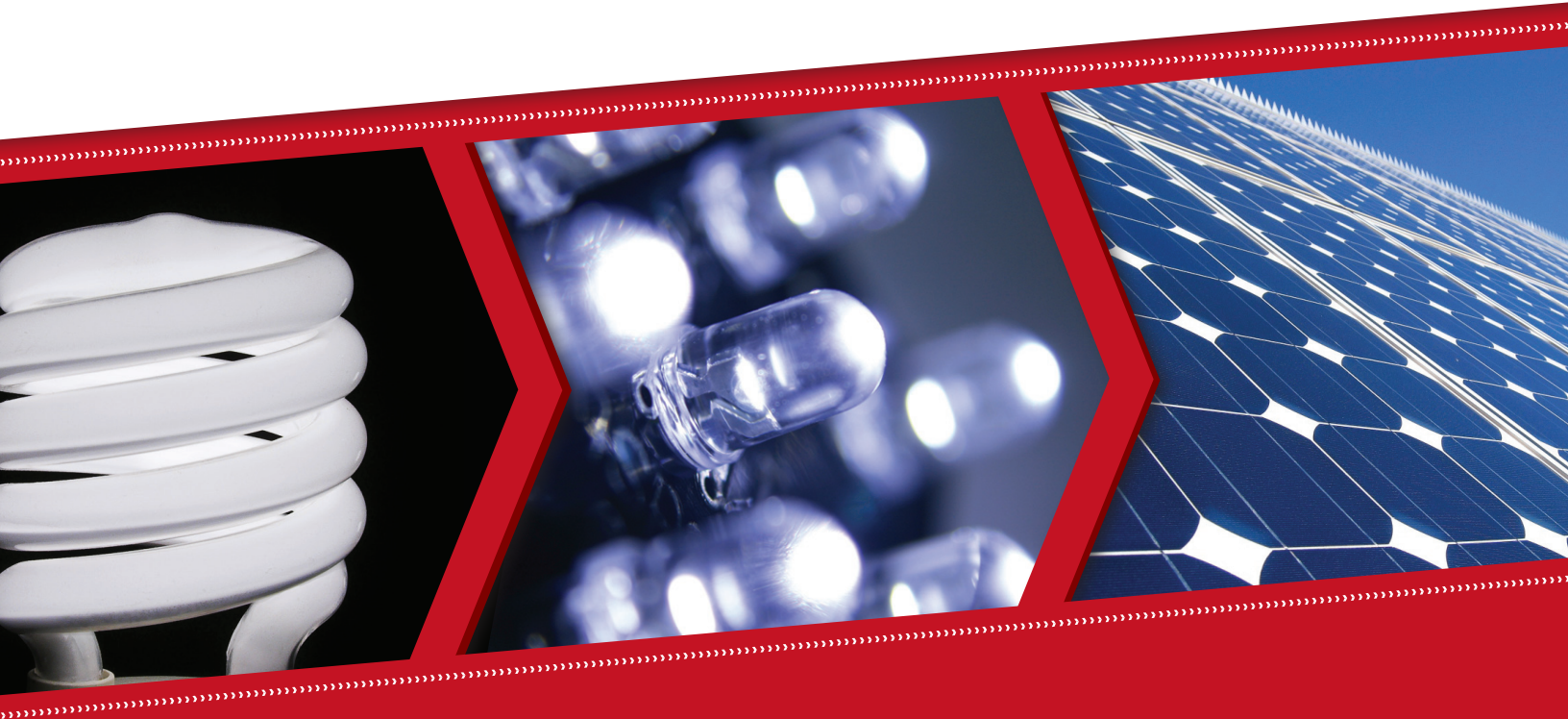


# Executive Summary



EDUCATION &  
RESEARCH FOUNDATION



# FRIEND OR FOE?

*Energy Services Companies and the Electrical Distribution Industry*

Prepared for:  
National Association of Electrical Distributors

Funded by:  
Channel Advantage Partnership

Prepared by:  
Vermont Energy Investment Corporation

# ESCOs: Friend or Foe?

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NAED Education & Research Foundation's Channel Advantage Partnership.

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Researched by Vermont Energy Investment Corporation

## Executive Summary

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# 《Executive Summary

## 《Background》

This study was intended to describe the energy service company (ESCO) industry and identify best practices for distributor-ESCO relationships, including how NAED members can best negotiate relationships with the different types of ESCOs.

The findings of this research establish that the ESCO industry is large and growing. Further, it identifies opportunities for NAED members to secure more energy efficiency retrofit work through either partnerships with ESCOs or by working independently, though both approaches carry risk and must be carefully assessed. This report identifies specific recommendations for NAED members to help them assess that risk and secure positive and profitable working relationships with ESCOs.

## 《Key Findings》

- » An ESCO is broadly defined as a business that develops, installs, and arranges financing for projects designed to improve the energy efficiency while lowering building maintenance costs. ESCOs typically work in existing buildings, rather than the new construction market, which has little need for ESCO services. The key distinguishing component of an ESCO's business model is the performance-based contract, which ties the ESCO's compensation to the amount of energy that is actually saved through the project.
- » ESCO market revenues exceeded \$5.1 billion in 2011, largely attributable to the increase in federal mandates on energy savings and increased push towards performance contracting. Aggressive growth scenarios project a compound annual growth rate (CAGR) of 14% and revenues of \$16 billion by 2020.
- » Energy efficient products comprise 75% of ESCO revenues, and 73% of revenues come from the Municipal, University, School, and Hospital (MUSH) market sector.
- » Large ESCOs tend to seek jobs above \$1 million in total project cost, which leaves significant opportunities for distributors to work on efficiency retrofits that are smaller in size.
- » ESCOs see themselves in the business of providing value added services and making return on investment (ROI) based sales to customers. They would value a greater focus on ROI sales from the electrical distribution industry.
- » 47% of NAED member distributors surveyed viewed ESCOs as competitors. Among distributors that have worked with ESCOs, the vast majority glean 10% or less of their total project revenues as the result of ESCO partnerships. However, a sizeable percentage (44%) indicated that they are actively targeting ESCOs as partners or customers.
- » Challenges in negotiating successful partnerships with ESCOs include developing true partnerships, margin, owning the order, and having the right expertise for the job.
- » Interviews with ESCOs, electrical contractors, and electrical distributors indicate that there are several types of partnerships that electrical distributors may want to pursue outside of the Super 16 ESCO companies. More promising targets include smaller regional or local ESCOs and electrical contractors that work with the Super 16 ESCO companies. Electrical distributors can increase their value to ESCOs—and also to customers that are interested in efficiency upgrades—by developing a sales force with a higher caliber of training on new, efficient technologies and products than the typical distributor salesperson.
- » Holding memberships at organizations such as the International Association of Lighting Management Companies (NALMCO) and the National Council on Qualifications for the Lighting Professionals (NCQLP) can facilitate the creation of successful ESCO partnerships. These organizations seek to develop relationships across the lighting industry, as well as ensuring minimum standards of quality through certifications; both of which can play a key role in aligning distributors with ESCOs that have similar values and skills.

## 《Selected Recommendations》

This report includes many recommendations for NAED members who are seeking advice on how to assess ESCOs and negotiate successful partnerships with them. A few highlights are included here.

The most important of the report's recommendations is to scan the market regularly for ESCO activity and to proactively develop a strategy outlining whether, and if so how, the NAED member will engage with ESCOs.

If the NAED member's strategy is to seek partnerships with ESCOs, it must assess potential partners carefully. A process is presented on page 42 of the full report that will help to ensure that the experience is a positive one. In seeking partners, the NAED member will need to clearly articulate its value and what it would bring to the ESCO. Many ESCO interviewees indicated that by far the highest value they get from distribution is lead generation. Therefore, the NAED member should be prepared to ask for higher margins and reap the rewards of bringing a lead to an ESCO and also mention the other values that distribution provides, namely technical product knowledge, logistical and supply chain services, and financing of product costs.

If the NAED member's strategy is to avoid working with ESCOs and pursue energy efficiency upgrades independently, the first step is to become aware of all relevant incentives, loans, and rebates that can be brought to bear on a particular job. The member should also mine past and current clients for retrofit opportunities, and train salespeople to be more than order takers; train them on the latest technology and how to develop and close deals based on ROI (return on investment).

## 《Research Goals and Methodology》

THE GOALS OF THIS RESEARCH PROJECT ARE TO:

- » Define categories that capture the different types of ESCOs currently in operation
- » Identify best practices for distributor-ESCO relationships
- » Uncover how NAED members can best negotiate relationships with the different types of ESCOs
- » Outline critical measures to help ensure that working with an ESCO will prove profitable for distributors
- » Provide an overview of the key elements of ESCO building energy efficiency projects, including financing, performance guarantees, project management, and installation of measures

To inform the recommendations in this white paper, VEIC conducted secondary and primary research. The secondary research included reviews of reports by market research firms, the Department of Energy, and Lawrence Berkeley National Laboratory, as well as web-based research. In the area of primary research, VEIC fielded a web-based survey of the NAED membership and conducted phone interviews. The primary research is further described below.



In the spring of 2012, a survey questionnaire was sent by internet to 690 NAED members, 230 of which were associate or allied members (*i.e., manufacturers*). The questionnaire was conducted over the internet utilizing the survey software of a leading research provider (*SurveyMonkey.com, LLC*). Over a three-week period 95 usable returns were obtained, yielding an overall response rate of 13.8 percent. The response rate was higher for distributors (15.9%) than manufacturers (9.6%). Due to the nature of the NAED membership and goals of the survey, this difference in response is not unexpected.

VEIC also conducted phone interviews with ESCOs, electrical contractors, and NAED members. VEIC performed 11 phone interviews with ESCOs and electrical contractors during the month of April 2012. In addition, VEIC conducted 14 phone interviews with NAED members (both distributors and manufacturers) in May and June 2012.

The complete report is available to NAED members on the [NAED Learning Center](#). For more information, contact NAED Member Services by email at [memberservices@naed.org](mailto:memberservices@naed.org) or by phone at 888-791-2512.

## «Channel Advantage Partnership

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