

Business, Energy and Industrial Strategy Committee Inquiry into Energy Efficiency

Energy UK response

17th January 2019

Introduction

1. Energy UK is the trade association for the GB energy industry with a membership of over 100 suppliers, generators, and stakeholders with a business interest in the production and supply of electricity and gas for domestic and business consumers. Our membership covers over 90% of both UK power generation and the energy supply market for UK homes. We represent the diverse nature of the UK's energy industry – from established FTSE 100 companies right through to new, growing suppliers and generators, which now make up over half of our membership.
2. Our members turn renewable energy sources as well as nuclear, gas and coal into electricity for over 27 million homes and every business in Britain. Over 680,000 people in every corner of the country rely on the sector for their jobs, with many of our members providing long-term employment as well as quality apprenticeships and training for those starting their careers. The energy industry invests over £12.5bn annually, delivers around £84bn in economic activity through its supply chain and interaction with other sectors, and pays £6bn in tax to HMT.
3. These high-level principles underpin Energy UK's response to the Business, Energy and Industrial Strategy Committee's inquiry into the Government's approach to delivering energy efficiency improvements to buildings. This is a high-level industry view, and Energy UK's members may hold differing positions on particular issues.

Executive Summary

4. Energy UK welcomes the opportunity to provide evidence on the Business, Energy and Industrial Strategy Committee's Inquiry into Energy Efficiency.
5. We have been pleased to see commitments from Government in recent years to supporting energy efficiency in homes and businesses in the UK. In order to meet the Government's 2050 carbon goals, it is clear that alongside a shift to cleaner sources of power generation, it is necessary to optimize how we use energy.
6. We welcome the Government's ambition to create an able to pay market for energy efficiency, as well as the targets set out in the Clean Growth Strategy (CGS). While the targets are welcome, we consider more detail is needed to outline how they will be met. There is currently a lack of specific detail from government about how it will achieve its targets, as well as a significant funding gap, estimated at around £4.5bn by the Energy Efficiency Infrastructure Group, between what is currently being delivered, and what is required to meet these targets. We also support more ambitious regulations to drive demand in energy efficiency.
7. This is a sizeable task, and we acknowledge that commitment from Government, the industry as well as households and businesses is needed to drive meaningful change in efficiency. Larger suppliers have a long history of delivering energy efficiency measures through obligations, and are set to deliver measures to around 1 million households by 2022 under the current phase of the

Energy Company Obligation (ECO 3). However, obligations alone were not designed to produce the delivery of measures to meet the level of change needed.

8. There are a number of disadvantages to the supplier obligation model. It has led to an overreliance by the supply chain on ECO funding and suppressed demand for measures from the able-to-pay market. As it is funded via consumer bills, the model is also regressive, meaning low income and fuel poor households contribute as much towards ECO as higher income households, and many do not receive any assistance through the scheme. Commercial realities also mean the scheme is delivered on a 'least-cost' basis, which is better suited to low-cost measures and easy to treat homes, but falling short effective support for the fuel-poor who tend to reside in lower quality and harder to treat dwellings.
9. Energy UK, therefore, strongly believes that after the conclusion of ECO 3 in 2022, support for fuel poor customers should move into general taxation. Furthermore, government needs to do more to help an able to pay market for energy efficiency measures, in both the domestic and non-domestic sectors, become sustainable.
10. Support will be needed from Government, industry as well as the able-to-pay market to make progress in energy efficiency. We support:
 - A strong Government commitment to build a market for energy efficiency, through ambitious timebound regulations on both domestic and non-domestic building, as well as new builds.
 - Development of detailed policy to set a path to achieve the targets set out in the CGS.
 - Development and promotion of incentives that encourage and support building owners to adopt energy efficiency measures in advance of regulatory requirements.
 - Government-funded support for those in fuel poverty and less able to contribute to energy efficiency improvements.
 - A strong foundation in the quality and standards of energy efficiency measures to maintain public trust and confidence.

Detailed responses to questions

Overarching approach: Who should have responsibility to pay for energy efficiency? Should energy efficiency be considered a national infrastructure priority?

11. Energy UK members have a long history with delivering energy efficiency through obligations, where suppliers are required to promote energy efficiency measures in domestic premises. The UK Government has placed obligations on suppliers to promote the installation of energy efficiency measures since 1994. The latest obligation, ECO 3, is worth approximately £640m a year and is due to run until 2022. In recent years the number of obligated suppliers has grown as new players have entered the gas and electricity market, and 14 suppliers are now covered under the obligation.
12. While our members take their responsibilities through ECO seriously, we note that there are downsides to funding energy efficiency measures through a supplier obligation:
 - The supply chain has largely become dependent on subsidies, rather than developing ways to sell energy efficiency measures. As a result, consumers across income scales have come to expect the delivery of measures at no cost. This has led to delivery being constrained to those actively funded through ECO and other subsidised schemes.
 - ECO is designed to incentivise suppliers to deliver a high volume of energy efficient measures for the lowest cost. The shift to require 100% of the obligation to be delivered to affordable warmth category homes create challenges within the scheme. Much of the 'low hanging fruit' in terms of low-cost, easy to install measures have been completed.

Remaining measures are more likely to be higher cost measures, such as solid wall insulation, or be delivered in remote and rural households, which increases per-measure costs. This approach has also increased the amount spent on search costs.

- Funding for ECO is derived from the energy bills of all customers, meaning that even those on low incomes who are least able to pay, and may not receive measures, are paying the same amount towards the Scheme as all other customers. This approach is regressive, and disproportionately hurts households in vulnerable circumstances and fuel poverty. In 2018, the UK Energy Research Centre found that the poorest households contribute £271 million per year towards energy policy costs, while in 2016/17 the cost of the Carbon Savings Communities and Affordable Warmth Schemes was £220 million. The poorest households are effectively self-funding initiatives intended to support them.¹
 - The original framework for energy efficiency obligations on suppliers was designed to create a reliable market for new and innovative energy efficiency measures to demonstrate viability and encourage further uptake in the able-to-pay space. The Centre for Sustainable Energy noted that obligations were a key driver of the adoption of energy efficiency measures such as cavity wall insulation, loft insulation and low energy lightbulbs.² As the targets and intended recipients of support have increasingly included social goals (such as targets for the fuel poor and rural areas), obligations have been more complex and difficult to administer, while underutilising the value the industry can bring to supporting new technologies and innovation.
13. Energy UK believes that it is important to support households in fuel poverty, and for the reasons outlined above, supports the Government, funding energy efficiency measures through general taxation after the end of ECO3 in 2022. The Government should develop a centrally-funded national energy efficiency scheme to improve the quality of UK homes for those in or at risk of fuel poverty. The Government scheme could make use of administrative data similar to the Department of Work and Pensions data-match for the Warm Home Discount broader group, to streamline the process of identifying and supporting households in fuel poverty.
14. We also acknowledge that households and firms will need to take steps themselves to become more energy efficient, and we consider that more should be done to encourage households and firms to place value on energy. Previous steps to stimulate a market for energy efficiency measures for 'able-to-pay' households, such as the introduction of minimum energy efficiency standards for privately rented buildings has had limited success in creating a functioning private market for energy efficiency measures. Action needs to be taken to set clear pathways and expectations.
15. To support the development of an energy efficiency market, we believe Government needs to make sure that the recommendations of the Each Home Counts Review are implemented to ensure quality, standards and accreditation is governed by a single framework. This framework has the potential to transform the market for retrofit energy efficiency measures and improving overall quality and safety by requiring all work to be delivered through the TrustMark Framework, ensuring high levels of workmanship and customer satisfaction.
16. We would encourage the Government to make energy efficiency a National Infrastructure Priority in the same way as the Scottish Government. This would send a clear signal that the Government recognises the importance of energy efficiency in meeting its CGS and carbon reduction targets, and demonstrate the need for multiple solutions to deliver the level of change needed.

¹Barrett J, Owen A and Taylor P (2018) Funding a Low Carbon Energy System: A fairer approach?, UK Energy Research Centre, <http://www.ukerc.ac.uk/publications/funding-a-low-carbon-energy-system.html>

² Centre for Sustainable Energy (2014), Beyond the ECO: An exploration of the options for the future of a domestic Energy Supplier Obligation. <https://www.cse.org.uk/projects/view/1257>

Existing housing stock: *Are the Government's targets to improve the Energy Performance Certificate (EPC) ratings of our existing housing stock ambitious enough? Is there sufficient support in place to deliver targets for all homes to be EPC band C by 2035? Is the Energy Company Obligation (ECO) an adequate mechanism to ensure fuel-poor homes are upgraded to EPC band C by 2030?*

17. Energy UK has welcomed the targets set out in the CGS to improve the EPC ratings of the existing housing stock and believe that clear, measurable and enforceable targets are necessary to drive change in energy efficiency. However, we support more ambitious targets than those set out in the CGS, as well as detailed policy to set out how the targets are going to be achieved. We do not consider ECO is sufficient to ensure fuel-poor homes are upgraded to EPC band C by 2030.
18. ECO is effectively the only driver of energy efficiency in the private domestic sector, and there is a significant gap in funding between energy efficiency measures being provided, and what is needed to reach the Government's targets. A recent report by Frontier Economics on behalf of the Energy Efficiency Infrastructure Group (EEIG), estimated that to meet the UK's 2035 targets there is a £4.5bn per year investment gap that needs to be filled via a combination of new private funding and increased public funding.³
19. To support households to comply with stricter regulatory requirements, and encourage uptake ahead of timeframes, the Government should consider what incentives it can put in place to provide a pathway to meeting the standards.
20. Energy UK and others have previously identified a number of initiatives that government may wish to consider to form part of a scheme to kick-start the able-to-pay energy efficiency market.⁴ Of the options presented, we believe that adjusting the Stamp Duty of a property for house movers in accordance with its EPC is worth particular consideration and should be one key initiative in any future policy framework. This could be revenue neutral for the Treasury but would provide an incentive and value for customers to install energy efficiency measures.
21. Opening the financial market to mechanisms beyond the Green Deal would also be welcome. Under the right circumstances, a 'Pay As You Save' mechanism could still provide customers with access to the funding needed to improve their properties and minimise the disincentives presented by large upfront installation costs.
22. The combination of incentives and regulations should also help drive a clearer link between energy efficiency investment and increased property value, i.e. via higher EPC ratings. If home or property owners can see a clear value to having a higher EPC value from either the additional leveraging of finance or reduction in stamp duty, it would help to increase interest in improving the overall efficiency of the home.

Private rented sector: *Are the Government's private rented sector regulations for energy efficiency for both residential and commercial buildings ambitious enough? Are there implementation and enforcement challenges that need to be remedied?*

23. We welcome the Government's recently announced changes to minimum energy efficiency standards in the domestic private rented sector (PRS), including increasing the cap on financial contributions from landlords to fund energy efficiency measures to £3,500. However, we also note that BEIS expects just 48% of domestic EPC band F or G PRS properties to be upgraded to EPC

³ Frontier Economics (2017), Affordable warmth, clean growth, <http://www.frontier-economics.com/uk/en/news-and-articles/articles/article-i4324-affordable-warmth-clean-growth/>

⁴ Energy UK, "Kick-starting a sustainable energy efficiency market", October 2015

band E or higher by 2020 through the regulations.⁵ We would support more ambitious minimum standards to drive more privately rented dwellings to become more efficient, and would support a target to reach EPC ratings of C and above.

24. Even with more ambitious regulations, adequate enforcement is needed to ensure action is taken. There have been a number of implementation and enforcement issues with the existing regulations:
- **Provide significant leeway for exemption**, a view backed up by 56% of respondents to a recent survey.⁶
 - **Have insufficient enforcement and compliance**. The Committee on Climate Change (CCC) quote in their summer update a recent Environmental Industries Commission report suggesting that businesses are not making the EPC available in the first place and fines are not being issued for non-compliance.⁷
 - **Exclude large industrial buildings** covered by the EU Emissions Trading Scheme and/or Climate Change Agreements.
25. While we support more ambitious targets to drive the necessary change needed to increase uptake in energy efficiency, we consider that better enforcement of the existing regulations would undoubtedly help to ensure landlords are meeting their obligations.

Regional disparities: *Are there regional disparities, including in off-grid areas, in the delivery, costs and uptake of energy efficiency measures? If so, how could these be overcome?*

26. Yes, the experience of suppliers delivering energy efficiency measures in rural, remote and island communities is that higher costs are involved in all stages of delivery, including:
- the initial search costs of identifying eligible households.
 - assessments by installers to verify the appropriateness of particular measures in a household.
 - the costs of transporting materials and installers to more remote areas to carry out installations.
 - technical monitoring and quality assurance inspections.
27. Scotland and Wales have been particularly successful in supporting the delivery of measures to rural areas. This is discussed in the 'lessons to learn' response below.

Non-domestic sector: *What does existing evidence indicate about progress being made towards greater energy efficiency in public and commercial buildings?*

28. The UK does not currently have a plan, nor the policy instruments, in place to deliver the 20% increase in energy productivity among non-domestic users cited in the CGS. There is evidence that a number of barriers exist in the non-domestic sector to improving the energy efficiency of commercial buildings, including:
- Lack of access to capital.
 - High upfront costs for energy efficiency measures and long payback periods, reducing the relative attractiveness of energy savings, particularly for new businesses that may consider a change in premises within the payback period.
 - Misaligned incentives between tenants, who typically accrue the benefits of energy efficiency measures, and landlords, who fund them.

⁵ DOMESTIC RENTED SECTOR MINIMUM LEVEL OF ENERGY EFFICIENCY Government Response to the consultation on proposals to amend The Energy Efficiency (Private Rented Property) (England and Wales) Regulations 2015, https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/753710/Final_PRS_Minimum_Standards_Consultation_Government_Response.pdf

⁶ EEVS insight and Bloomberg New Energy Finance (2017), *Energy Efficiency Trends Report Vol. 21*, <http://www.eevs.co.uk/pastreports.html> (Q3 2017)

⁷ Committee on Climate Change, Reducing UK emissions, 2018 Progress Report to Parliament, June 2018

- Disruption to normal business activities while retrofitting is taking place.
 - Competing priorities. Evidence indicates that businesses where energy use is a low proportion of their overall cost structure are less likely to consider improving their energy efficiency due to the relative benefit of doing so.⁸
29. A vibrant energy services industry can and should help to address many of the barriers to businesses undertaking energy efficiency projects by helping to finance the high upfront costs and addressing lack of time and technical expertise. BEIS sponsored research has identified significant market potential in this sector.⁹ Incentives that tie energy efficiency to business rates, taxes or stamp duty would also help to encourage uptake in the non-domestic sector. Green building passports also show potential to facilitate pathways for firms to improve their efficiency incrementally over time.
30. Additionally, operational energy efficiency has received limited policy attention to date, as much of the focus has been on improving the efficiency of building fabric. There is a significant opportunity to drive further efficiency in the non-domestic sector by incentivizing firms to operate buildings to a high efficiency standard. This could be achieved through reductions in business rates, and providing tenants with information on a building's intended operational standard to ensure it is adequately maintained.
31. There are significant opportunities to improve energy efficiency in the non-domestic sector, however we do not support this being delivered through supplier obligations. Non-domestic buildings have far more variation in terms of building size, use and energy needs requiring a more tailored and bespoke approach. Obligations have worked best when measures are delivered at scale to encourage wider adoption. There is also a risk that an obligation would stifle the emerging energy services industry.
32. Through schemes like RE:FIT, we acknowledge that the public sector is already active in this space. In the tenanted commercial premises market, the public sector is thought to effectively set a floor for energy efficiency standards as well as act as a driver for the adoption of measures in private sector organisations. Larger commercial businesses are also showing interest, driven by the potential for cost savings, where the other potential barriers can be overcome.

Lessons to learn: What lessons can be learnt from the devolved administrations on delivering energy efficiency measures?

33. As previously mentioned, the Scottish Government has made energy efficiency a National Infrastructure Priority, which would be beneficial for the Government to follow suit to give a higher profile to the issue. Additionally, Scotland and Wales have developed programmes, supported by public investment, tailored for different scenarios.
34. Scotland and Wales have particularly focused on area-based delivery through initiatives such as the Home Energy Efficiency Area Based Scheme (HEEPS:ABS), Nest and Arbed. These programmes combine public funding and ECO, which helps to deliver economies of scale which is particularly important in rural areas helping to reduce some of the search and installation costs. This has also made it easier to carry out technical monitoring and quality assurance inspections on

⁸ Department of Energy and Climate Change (2012) – The Energy Efficiency Strategy: The Energy Efficiency Opportunities in the UK https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/65603/6928-the-energy-efficiency-strategy-statistical-strat.pdf

⁹ IPA Advisory Ltd, The non-domestic energy efficiency services market, 2018, <https://www.gov.uk/government/publications/non-domestic-energy-efficiency-services-market>

a number of properties in an area. A high proportion – 13% of all measures delivered under ECO2 were in Scotland.

35. Scotland and Wales have also provided a key role in promoting energy efficiency measures through a central helpline which is likely to have increased the uptake of measures. This demonstrates the need to ensure advice and support are made available for consumer including that the advice needs to be specific and impartial. The devolved nations have also played a key role in raising awareness of their schemes and promoting them to households encouraging them to take action to improve the energy efficiency of their homes.
36. The Government should look at ways to build on this success, following on from the examples in Scotland and Wales.

For further information or to discuss our response in more detail please contact Steve James on 020 7747 2969 or at steve.james@energy-uk.org.uk.