



# Addressing the Able to Pay Sector

Update on Energy Efficiency Policy 2020



SUSTAINABLE  
ENERGY ASSOCIATION

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# Introduction



In 2017, the Sustainable Energy Association (SEA) published a report titled [Energy Efficiency - A Policy Pathway: Addressing the Able to Pay Sector](#). It outlined the homeowner's tendency to delay decision making around energy efficiency upgrades and proposed several policy interventions to address this. This paper revisits the recommendations made in 2017 and discusses their continued relevance for the UK.

Since publication, the policy landscape has evolved but the saliency of these recommendations has only grown. In 2017, the Government released a [Call for Evidence on Building a Market for Energy Efficiency](#), focussing specifically on the able to pay sector. Two years later, the Government legislated the 2050 net-zero target, which will necessitate significant action to decarbonise the UK's 29 million homes. Energy use in homes accounts for around 14% of UK greenhouse gas emissions so addressing this area is crucial to meeting the country's climate change targets.<sup>1</sup> In the same year, the Government released its [Green Finance Strategy](#) outlining its desired direction of travel for the sector. Throughout this period industry bodies have issued calls for action to 'green' the property sector to drive demand<sup>2</sup>. However, the overarching policy environment for owner occupied housing has remained relatively unchanged.

In response to Covid-19, the Government announced the Green Homes Grant, where

homeowners receive up to £5,000 (£10,000 for fuel poor households) to cover the cost of energy efficiency measures. Whilst this is a welcome initiative in providing short term stimulus to the market, it needs to form part of a broader policy framework to ensure sustainable growth. Energy efficiency can get the UK back to work after Covid-19, but it has greater potential as a growth market compatible with the Clean Growth Strategy. Working patterns have changed irrevocably as more people than ever now work from home. Nine out of ten employees who worked at home during the UK's lockdown would like to continue working at home in some capacity, with almost half (47.3%) keen to work at home often or all the time<sup>3</sup>. An opportunity exists to develop a new narrative where energy efficiency is central to a comfortable living and working space. This could be a powerful message if used in tandem with the recommendations discussed below. Those who have shifted to home working patterns may have realised savings from reduced transport costs and they should be encouraged to use these for home improvements like insulation or ventilation. With the Energy White Paper and the Heat & Buildings Strategy due for publication this Autumn, now is an ideal time to consider what actions are needed to drive energy efficiency improvements on the able to pay sector.

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<sup>1</sup> Committee on Climate Change; 2016; UK Homes: Fit for the Future? Available at: <https://www.theccc.org.uk/wp-content/uploads/2019/02/UK-housing-Fit-for-the-future-CCC-2019.pdf>

<sup>2</sup> Green Finance Institute; 2020. Stimulus actions for a greener and more resilient property market. Available at: <https://www.greenfinanceinstitute.co.uk/report-stimulus-actions-for-a-greener-and-more-resilient-property-sector/>

<sup>3</sup> Felstead & Reuschke; 2020; Homeworking in the UK: Before and During the 2020 Lockdown. Available at: <https://wiserd.ac.uk/publications/homeworking-uk-and-during-2020-lockdown>



# A Deficit of Demand in the Able to Pay Sector

Reducing energy use and thermal efficiency is most challenging in the owner occupier sector, where there are more poorly performing buildings than in privately rented properties or in social housing. The lengthy payback periods and consumer tendency to discount future benefits stymie demand from this customer segment, at a time when the UK must retrofit most homes to meet net-zero by 2050.

Homeowners can be encouraged to install energy efficiency measures at certain trigger points; at the point of sale or purchase of a property, or even during major renovations. Many of the following recommendations transform these trigger points into opportunities where the homeowner is enabled or nudged towards installation of energy efficiency measures.



# Energy Performance Certificates (EPCs)



Many of the recommendations outlined in this paper integrate EPCs into their delivery. The EPC has evolved significantly since its conception. Initially, it was an ‘asset rating’ metric, designed to serve as an indicator of the cost of running a home, but has become a tool in policy making, underpinning mechanisms such as the Renewable Heat Incentive, Feed-in-Tariffs and the Energy Company Obligation. Despite this central role, different EPC ratings could be generated by different independent assessors for the same building. Inaccuracies are exacerbated by the ten-year lifespan of EPCs, during which time, a host of changes could be made to the building making the EPC outdated. EPC assessors recalculating the rating do not have access to all the data used for the original assessment so recalculate measurements or make new assumptions. They are often pressured to calculate ratings quickly and the need to replicate multiple calculations can be an issue. This could lead to assessors selecting defaults rather than being accurate in their measurements. Furthermore, measures that improve the Energy Efficiency Rating and improve a building’s EPC can simultaneously worsen its Environmental Impact Rating.

Whilst improvements to the EPC calculation methodology are needed, the Government also needs to promote traceability and use of real time energy performance data. In new build homes, the gap between specified and actual energy efficiency performance ensures that EPCs are not a true reflection of building fabric performance. In some cases, ‘best in class’ products are specified at design stage, but during construction lower performing, cheaper solutions are used. This creates misleading energy performance ratings and can lead to sub-optimal performance. This was addressed by the Hackitt Review which called for the creation of a ‘golden thread’ of information tracing a building’s history. In this context, a digital ‘Buildings Passport’ would provide an accessible location for home EPC information which could host all the relevant information and building history. The Call for Evidence closed two years ago yet the Government is yet to respond. With suitable reform, EPCs can be creditably used to underpin the below policy interventions, but the Government needs to set out how this metric will be improved.

<sup>4</sup> BEIS; 2018; Energy Performance Certificates in buildings: call for evidence; Available at: <https://www.gov.uk/government/consultations/energy-performance-certificates-in-buildings-call-for-evidence>

<sup>5</sup> BEIS; 2018; Energy Performance Certificates in buildings: call for evidence; Available at: <https://www.gov.uk/government/consultations/energy-performance-certificates-in-buildings-call-for-evidence>



# Recommendations



# Policy Drivers

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The Green Homes Grant is a timely intervention in the market. However, subsidies alone will not be sufficient to drive significant deployment of energy efficiency measures. Government needs to introduce both policy drivers and policy enablers to ensure that homeowners are encouraged and able to carry out energy efficiency improvements. The following policy drivers could create long term, sustainable demand in the able to pay sector. Further details of each proposal can be found in the full 2017 [report](#).

## VARIABLE STAMP DUTY

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The flexing of stamp duty would see houses scored based on the property's SAP rating and the tax would vary accordingly. In targeting the loss aversion of homebuyers, flexible stamp duty could encourage the public to buy more efficient properties. This idea has been implemented in the past with the Government removing stamp duty on zero carbon homes worth under £500,000. To encourage the uptake of retrofits, rebates could be offered for households that conduct EPC recommended improvements within 12 months of entry. The policy could utilise RdSAP points of 0-100 to reduce the risk of distorted assessments at the edges of EPC bands. Using EPC band C as a target, scenario planning indicated that the Government would receive £742m in additional revenue.

Over time, house prices are likely to adjust to reflect the energy efficiency rating of the property which would provide an additional motivation for buyers to opt for higher efficiency properties or carry out improvements during their ownership. The policy would be designed to be revenue-neutral for the Treasury in the long term, as reduced tax income raised from efficient houses would be sourced from less-efficient properties.

In temporarily relaxing stamp duty as a response to Covid-19, the Government has displayed its political willingness to amend rates. Having made such an intervention already, the Government should be open to conducting further experimentation with stamp duty. A trial could potentially be run in partnership with the Scottish Government who control their own rates through the [Land & Buildings Transaction Tax](#). For example, a pilot could vary the rate paid on the Additional Dwellings Supplement (paid by homeowners on every second property) according to energy efficiency, to test

## CONDITIONAL MORTGAGES

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There are multiple ways that mortgages can drive energy efficiency; granting of a mortgage on the condition that home improvements are carried out, or the granting of larger mortgages based on the energy efficiency rating. A mortgage could be issued based on a property's current energy performance level, with higher mortgage offers for A-C rated properties. The lower running costs of highly efficient properties reduces the likelihood of defaulting on mortgage repayments and can create a virtuous cycle, where lower bills allow for bigger mortgage repayments and consequently increased lending from banks. Since publication of our 2017 report, [further evidence](#) has emerged that the energy efficiency of a property is a relevant predictor of mortgage risk. Mainstream banks such as [Barclays](#) and [Nationwide](#) have begun to offer green mortgages which reward households for purchasing more efficient properties but wider uptake is now needed in the market. However, the market remains relatively undeveloped and inflexible. For example, the Barclays offering is only eligible with new homes.

Alternatively, mortgage lenders could offer more favourable rates on the condition that improvements are made, which would incentivise post-sale refurbishments. In most cases, a mortgage pre-approval application will be marked as 'approved with conditions'. To get loans approved buyers must already meet a range of conditions, such as carrying out surveys and inspections or completing repair work. Therefore, adding energy efficiency improvements to the conditions on a mortgage should not be overly burdensome.

To support market development, data monitoring products could be used to test the real performance of energy efficiency measures, and this should provide further assurances for mortgage providers. The Government has already supported product development through projects like the Smart Meter Enabled Thermal Efficiency ([SMETER](#)) Competition so deployment should be encouraged as a means to provide greater assurance for mortgage providers.

The Government has already committed £1.8 million through the Green Home Finance Innovation Fund. It aims to promote the establishment of green lending products for owner occupiers and mitigate initial development costs for financial institutions. The three supported projects are developing and piloting different green finance products that encourage retrofit in a variety of ways:

- Home Infrastructure Technology Limited (HIT) - Add to My Mortgage. This project is developing a digital platform that connects green vendors to mortgage lenders, allowing customers to search for energy efficiency measures that they would like to install in their homes. When the customer goes to pay for the chosen energy efficiency measure, the platform recalculates their mortgage to take into account the extra finance required to pay for it.
- Lloyds Banking Group (LBG) - Green Home Mortgage. An online home energy saving tool that allows visitors to their website to work out how energy efficient their homes are and create an individualised plan for home improvements. If the customer is prepared to go ahead with an installation the bank will offer either additional borrowing on their mortgage or a 'Green Home Mortgage' for new customers.
- Monmouthshire Building Society (MBS) - Valuations and Lending Underwriting Energy Reduction (VALUER). This project will develop a bundle including a mortgage product and an additional borrowing product to encourage customers to install energy efficiency measures. The borrowing rates will reflect the additional property value gained from reduced energy use.<sup>6</sup>

Such innovations are a step in the right direction, but further work and government support is needed to promote, commercialise and diversify such financial products.

<sup>6</sup> Green Homes Finance Innovation Fund-Successful Bids. Available at: <https://www.gov.uk/government/publications/green-home-finance-innovation-fund-competition-successful-bids/green-home-finance-innovation-fund-competition-successful-bids>



## COUNCIL TAX

It is believed that variable council tax could be a strong driver for action, as it has a high collection rate, a wide-ranging collection base, is levied and paid consistently and is a charge on the property itself. This mechanism would help to strengthen the link between the property value and its energy efficiency performance. With a clear connection established between energy efficient properties and lower council tax, this scheme could have large positive impacts in driving consumer demand for homes that have a good energy performance.

There are a range of methods to link council tax with energy efficiency improvements and the SEA report explored two; variable tax rates and rebates. Both offer the consumer the possibility of decreasing council tax outgoings through the adoption of energy efficiency or low carbon heating measures.

An increase or decrease to council tax could be issued depending on a household's EPC rating, as it relates to a dynamic baseline that reflects the average efficiency rating within a district. Households that install a cost-effective measure from their EPC would then see a corresponding decrease to their council tax. Though resource intensive to set up, this should encourage uptake of efficiency measures as house prices would likely increase over time dependent on the council tax savings that are achieved for a certain house. Long term, this could cause a societal shift towards valuing energy efficiency in our homes.

Alternatively, a one-off council tax rebate could be offered in return for the installation of energy efficiency measures. The rebate would be proportional to the cost of the measure to help households with the upfront costs. It is likely that a rebate would be simpler to administrate and progressive as council tax is applied to homes of all values. However, it would have a smaller impact on demand whilst potentially adding strain to council budgets.

Since publication, the Department for Business, Energy & Industrial Strategy (BEIS) has commissioned several feasibility studies on this topic, demonstrating the Government's openness to explore this driver. Council tax can be used in different ways to drive energy efficiency, but local authorities need support from government in doing so, either through providing an overarching framework, or in additional resources to aid implementation. Following these feasibility studies, BEIS should outline the next steps for policy in this area and work with interested local authorities on implementation and localised trials ahead of wider adoption.

## MINIMUM ENERGY PERFORMANCE CERTIFICATE AT POINT OF SALE

In the private-rented sector, Minimum Energy Efficiency Standards prevent the rental of homes that fail to meet a minimum EPC rating band E. For the owner occupier sector, a similar minimum EPC certificate could be brought in at the point of sale. A minimum standard of EPC band C would be suitable given the Government's target to upgrade all homes to this level by 2035.

In 2020, the Scottish Government consulted on introducing a mandatory EPC band C rating at the point of sale, as a regulatory mechanism to improve the energy efficiency of the building stock. This [consultation](#) outlined the potential regulatory framework and challenges associated with the policy, and this work should be built upon for a UK-wide regulation.

EPCs are a combination of an Environmental Impact Rating (EIR) and an Energy Efficiency Rating (EER). A 'fabric first' approach would be crucial to the success of this policy, as it would ensure that the EIR is not detrimentally impacted by improving the EER. Exemptions would be granted on technical feasibility, excessive cost, or failure to receive permission, as per regulations in the private-rented sector.

Crucially, the seller would retain the right to pass on responsibility for EPC improvements onto the buyer. The ability to pass on responsibility for improvements accounts for differing financial situations of buyers and sellers. What may not be cost effective for someone selling the property may be more realistic for a buyer. The new owner would be given a set time to make improvements, and this would need to be backed by stringent enforcement and appropriate penalties to drive compliance. Over time, the property value would reflect additional effort gone into upgrading the property before sale.

Following recent engagement with the Scottish Government on this consultation, the SEA would welcome the opportunity to share suggestions for the implementation of a UK-wide regulation. Although this proposal would require a lead-in time to develop the regulatory framework and build the supply chain for property assessments, the learnings taken from the devolved administrations and industry should streamline the development process.

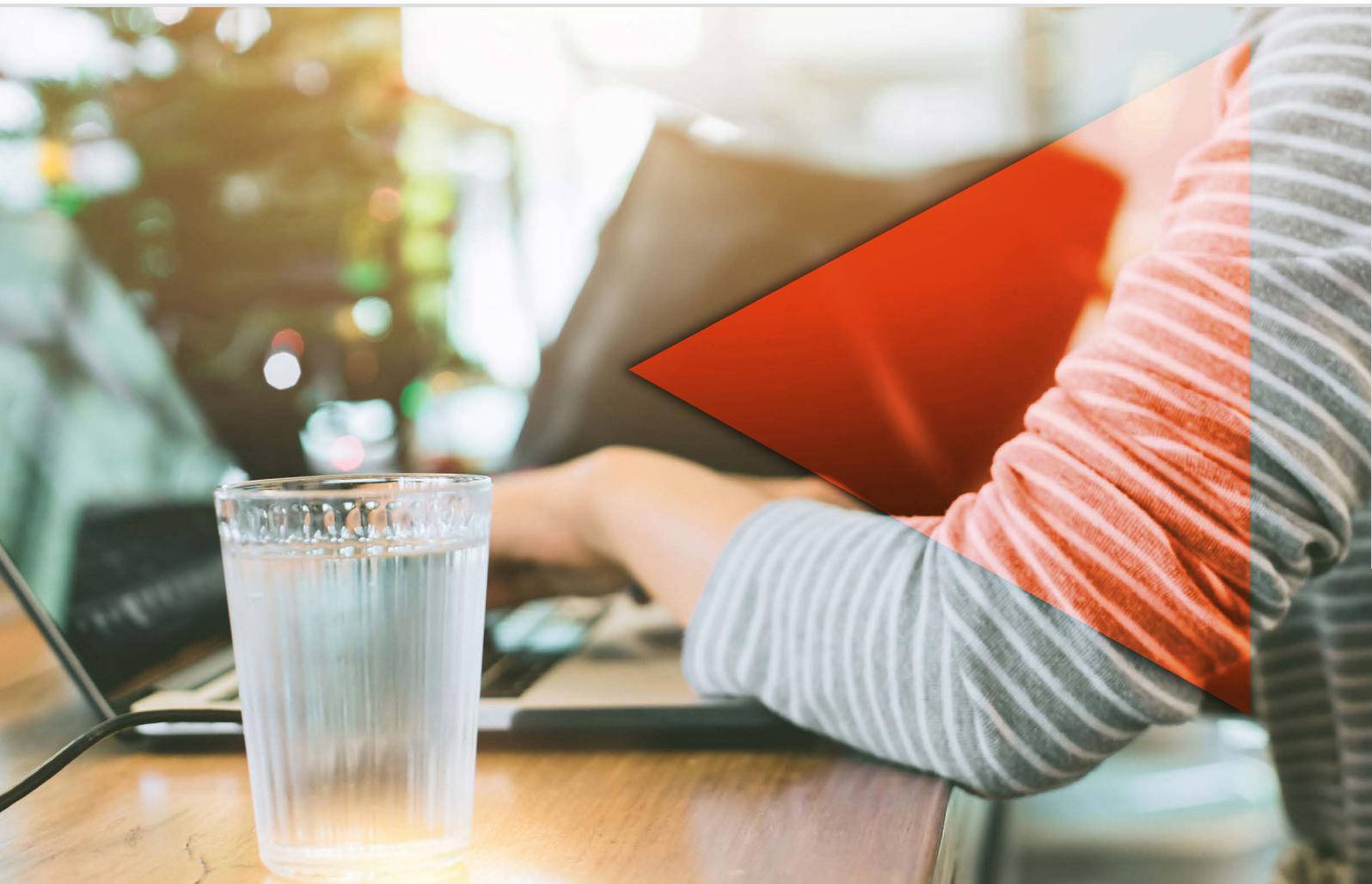




# Policy Enablers

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To support the above regulatory drivers, there must be the availability of financial support and mechanisms to enable households to invest in energy efficiency measures. The following section outlines three potential financial mechanisms which could be introduced alongside the regulatory nudges discussed above to overcome the high upfront costs and financial barriers faced by homeowners when considering energy efficiency improvements. Again, more detailed exploration of each is discussed in the original report.



## SAVING SCHEMES

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### Individual Savings Accounts (ISAs):

First time buyers are often unable or unwilling to invest significant sums in improving the energy efficiency of their property. Lifetime ISAs (LISAs) were introduced as a replacement for the Help to Buy ISA, which allow consumers to save £4,000 per year towards a first home or retirement, to which the Government adds a 25% bonus. Account holders face a penalty charge if they withdraw the money for any other reason, and this policy could be amended to permit penalty-free withdrawals for energy efficiency measures. This remains an unexplored and widely supported option within the industry. The Help to Buy ISA was first introduced in 2015 and has been phased out since the publication of the SEA's original report. However, the concept remains relevant to energy efficiency as it could be evolved into a 'help-to-renovate' savings account, where the Government top up could be tied to energy efficiency improvements.

### Help to Buy Scheme:

The Help to Buy Scheme offers a low-cost government loan towards the cost of new build homes. The [Green Finance Institute](#) has suggested that the current Help to Buy scheme 'be extended beyond new-build housing and repurposed to preferentially support first-time buyers to purchase an energy-efficient and resilient home, through minimum EPC criteria or government guarantees to support energy improvements once the property has been purchased'. Any future 'help to buy' type scheme could require developers to build to energy efficiency standards that are higher than specified in the Building Regulations, as a condition of accessing that support. Developers have benefitted hugely from the Help to Buy scheme, so it is unlikely they will oppose its continuation, albeit in an amended programme.

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<sup>7</sup> Green Finance Institute; 2020; Stimulus Actions for a greener and more resilient property sector. Available at: <https://www.greenfinanceinstitute.co.uk/wp-content/uploads/2020/06/Stimulus-actions-for-a-greener-and-more-resilient-property-sector-.pdf>

## HELP TO IMPROVE/ZERO INTEREST LOANS

Finance is a major barrier to the uptake of energy efficiency measures, and zero interest loans could make a powerful contribution in mitigating this. Such products are critical to creating sustainable demand long term in a post-subsidy environment. There is a risk that the Green Homes Grant will generate a boom and bust unless the Government commits to a successor scheme that gradually phases out subsidy. In parallel, financial mechanisms such as zero interest loans should be given greater emphasis and support to maintain the availability of finance. Customers without the required savings should be able to access low interest capital to undertake energy efficiency improvements. A number of countries have introduced interest free energy efficiency loans to overcome challenges around consumer finance:

- **Northern Ireland:** Businesses are able to access interest free, unsecured loans from £3,000 - £400,000 to fund energy efficiency or renewable energy projects. The finance is provided by the Government.
- **Scotland:** Owner occupiers and private sector landlords are able to access up to £15,000 per property to carry out efficiency measures with the repayment period varying depending on the amount borrowed. The finance is provided by the Government.
- **France:** Homeowners can take out a loan of up to €30,000 for home energy conservation other sustainability measures. The loans are provided by banks.
- **Germany:** Low interest loans provide homeowners the ability to carry out energy efficiency retrofits. The National Development Bank offers the loans through retail banks.

In many cases, the commercial banks are responsible for the application with government organisations providing the finance. The majority of these loans have a duration of approximately 10 – 15 years. The Government could set a maximum interest rate to ensure that homeowners are able to benefit from cheap finance.

In recent years, growing attention has been paid to the North American Property Assessed Clean Energy ([PACE](#)) model, widely adopted by states and provinces in the US and Canada. PACE programmes provide long term, low cost finance for clean energy and have succeeded where the UK's Green Deal failed. Banks provide long term capital for retrofit and local authorities or associated third parties collect repayments through an additional property charge that is passed onto the lender. This model has also been successfully used in Australia and could form the basis for a new financial support mechanism.

These products address the cost barrier for home improvements and allow the occupier to pay back over time and without undue financial strain, as energy efficiency improvements may lead to ongoing reductions in energy bills.

## EQUITY LOANS

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The SEA recommends the introduction of equity loans to allow homeowners to top up their mortgage to carry out home improvements, including energy efficiency works. Homeowners should be able to access an equity loan at any time to allow improvements to be made, for example, prior to marketing a property for sale. The UK Government should assess the feasibility of introducing a loan scheme similar to the Scottish Government's Home Energy Efficiency Programme for Scotland ([HEEPS](#)) Equity Loan Scheme. It should be designed to protect an individual's credit rating to ensure that an equity loan does not impede the ability of owner occupiers to borrow to pay for additional work to the property. Owner occupiers might use a range of finance sources for retrofit and renovation purposes, including housing-related finance such as advances on an existing mortgage or equity release. A green equity release would allow homeowners over the age of 55 to unlock equity in their property without having to move. This would include favourable terms to incentivise retrofit and the ability to protect the property's value. Such a scheme offers finance routes for a specific demographic who potentially may have limited access to alternate resources<sup>8</sup>.

## Conclusions



It is widely accepted that homeowners are unlikely to carry out energy efficiency improvements of their own accord. This paper has outlined a range of market-based and scalable policy interventions to help invigorate the able to pay market and encourage the uptake of energy efficiency measures. Since publication of the SEA's original report, further evidence has emerged supporting the continued relevance of these recommendations. However, they have remained largely unexplored by the Government, even though energy efficiency will be central to decarbonisation of the UK's building stock. A range of solutions will be needed to increase demand in the owner occupier sector, reflecting the variation in circumstance, means and motivation of homeowners. The SEA calls on the Government to develop a robust framework to ensure that the able to pay market is incentivised and able to carry out energy efficiency improvements.

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<sup>8</sup> Green Finance Institute; Financing energy efficient buildings: the path to retrofit at scale. Available at: <https://www.greenfinanceinstitute.co.uk/wp-content/uploads/2020/06/Financing-energy-efficient-buildings-the-path-to-retrofit-at-scale.pdf>

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