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**Research project on home energy efficiency**

British Gas response to Bright Blue

May 2016

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## Questions

### **Question 1 – Why did the Green Deal fail? In particular, what mistakes were made in the design of the finance mechanism and the communication of the scheme?**

Supplier energy efficiency obligations have existed in the UK since 1994, and many householders have become used to the idea that energy efficiency measures – such as loft and cavity wall insulation – are provided for free. The Green Deal programme was predicated on the belief that further untapped consumer demand existed for energy efficiency measures, but was held back by the lack of a suitable finance product. Despite the introduction of Green Deal Finance, this assumed consumer demand failed to materialise.

While efforts by suppliers, Government and others in the supply chain to raise awareness of the Green Deal was largely successful, some consumers heard only negative stories about the scheme through the media, which coloured their perception of the programme, and made it less appealing. Furthermore, consumer awareness of the finer details of the scheme – such as how the finance would work, how repayments were made, and how to apply – was much lower, and this level of complexity put many consumers off.

In our experience, the Green Deal suffered from an over-reliance on Green Deal Finance to drive demand, a complex customer journey, and was hampered by the restrictive 'Golden Rule'. This constrained finance packages to only around 30% of installation costs, and those consumers who could afford to break the 'Rule' could generally access finance more cheaply elsewhere<sup>1</sup>.

Many householders were also put off by the perception of taking on debt. Our own research at the time indicated that many homeowners are debt averse and only 10 percent said they would consider using Green Deal Finance to pay for improvements. The majority - over 70 percent - said that they would pay for improvements from savings.

Many of those households who did take up a Green Deal Finance package invested in either a new boiler or photovoltaic solar panels. This suggests that many able-to-pay customers treat energy efficiency as either a 'distressed purchase' – in the case of boilers – or an investment – in the case of solar panels. Many other paid-for energy efficiency measures are generally not considered to be a good investment, as they may have a payback period in excess of ten years, and have little impact on property or rental values.

### **Question 2 – What aspects of the Green Deal scheme should be retained in a future policy?**

A successful paid-for market for energy efficiency improvements depends on the creation of significant consumer demand. Energy efficiency policy must take consumers as its starting point, and be built on a deep understand of their needs and behaviours. Our experience suggests that long-term demand for energy efficiency needs to be driven by incentives, regulation, or both.

While the pay-as-you-save model should be retained, but we do not believe that it will ever play more than a niche role, even with significant reform. The key benefit of pay-as-you-save is that it can provide finance to those who would otherwise struggle to borrow.

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<sup>1</sup> For example, Nationwide currently offers 'Green Additional Borrowing' to mortgage customers at an initial rate as low as 1.24% - far below the 8-12% APR typically offered by the Green Deal Finance Company.

The small numbers of finance plans delivered through the Green Deal were largely driven by incentives in the scheme; such as Cashback and the Home Improvement Fund. There is little evidence that the finance on its own caused consumers to take action.

We were disappointed by the early closure of the Green Deal Home Improvement Fund, as the overall approach was successful and created a compelling customer offer. However we recognise that it relied on significant taxpayer funding.

The creation of sustainable, long-term demand for energy efficiency measures can best be driven by a combination of both 'carrots' and 'sticks'. This could include taxpayer-funded offers, fiscally-neutral incentives such as variable stamp duty and council tax, or regulation; for example, by building on current legislation in the private rented sector.

**Question 3 – How should Green Deal-style loans for the able-to-pay sector be financed in the future? Is it necessary for the Government to provide any subsidy to the scheme?**

We do not believe that reforming the Green Deal Finance framework alone will lead to significant demand for paid-for energy efficiency measures. Instead, policy makers should focus on better understanding consumer demand, and the role that could be played by a combination of incentives and regulation.

**Question 4 - What lessons do you anticipate from the Bonfield Review about quality assurance in the supply chain? How can these be incorporated into a Green Deal successor scheme?**

PAS 2030 is a BSi standards document introduced for the supply chain installing energy efficiency measures under the Green Deal.

In our experience, the PAS 2030 system has insufficient arrangements for the monitoring of installations and consumer redress, and the scheme's penalties are not sufficiently punitive to disincentivise poor practice.

We believe that installation standards should be better enforced and more consistently upheld, with installers held accountable for the standard of their work, rather than those who contract with them – including energy suppliers.

We expect the Bonfield review to recommend the establishment of a new quality mark, overseen by a newly-created organisation similar to the Green Deal Oversight and Registration Body.

It is important that any new scheme avoids adding administrative burden. It should replace existing accreditation schemes rather than duplicating them. A new, more effective accreditation scheme would also reduce or remove the need for additional technical monitoring by Ofgem of measures installed under the Energy Company Obligation (ECO). This could reduce the overall cost of the scheme to billpayers.

**Question 5 - How can a Green Deal successor scheme be successfully communicated to consumers?**

If the successor scheme is sufficiently appealing, and the product is good enough to take to market, we believe that market participants should be allowed to communicate directly to consumers in the way they believe would be most effective. Government can also play a role in awareness raising, using a mixture of channels based on a thorough understanding of the target market audience and consumer demand.

The demand seen during the Green Deal was largely driven by incentives. Consumers were attracted by the 'Deal' in Green Deal, and acted if it was sufficiently compelling. For most, this meant cash-back or money off, and not a loan, however innovative. Energy bill savings alone are unlikely to persuade consumers to improve their homes.

For example, there is a vibrant and successful market for double glazing, where investments are not considered cost-effective in terms of energy bill savings alone, but are popular due to the potential to increase property value and other benefits, including noise reduction and reduced maintenance.

While tailored energy efficiency advice can also play a role in building remand, Green Deal assessments lack product information, a clear 'call to action' or advice on behaviour change. They are also lengthy, expensive, and can be intrusive.

Hundreds of thousands of Green Deal Assessments were carried out during the Green Deal programme, but there is little evidence that the assessments themselves created demand. In fact, the assessments were typically driven by the need to secure funding for installations that were already planned – for example, through the ECO or Green Deal Cashback.

We believe that consumer advice should be interactive, action-oriented and free. It could also be more targeted – for example, during the mortgage application or home buying process. We believe that an engaging online service could meet the needs of most consumers, and critically, should be based on a product that consumers actually want.

#### **Question 6 - What are the best options for decarbonising the domestic heat sector?**

The 2009 Renewable Energy Directive requires the UK to achieve 15% of its energy consumption from renewable sources by 2020. In 2009, the UK Government indicated that its target could be met through decarbonising 30% of electricity supply, 12% of heat demand and 10% of transport demand.

While there has been good progress made in deploying renewable power generation in recent years, progress in meeting heat and transport sub-targets has been slower. Unlike the current power generation sector, the heating and transport sectors are heavily decentralised and far more reliant upon individual actors to effect change. In both of these sectors we believe that the Government's focus should be on delivering cost-effective solutions which are attractive to consumers.

Making best use of the UK's existing gas network infrastructure is likely to be more cost-effective than pushing for the full electrification of both heat and transport sectors. Any cost-effective solution for heating will need to complement this existing infrastructure, and could involve the introduction of lower (or zero) carbon gases into regional networks where there is a positive business case to do so.

Decarbonisation could also be cost-effectively achieved with greater recognition of the role of gas technologies. Gas-fuelled Combined Heat and Power (CHP) plants are often the most appropriate technologies for district heating, and drive significant carbon savings where they replace electric heating.

Micro-CHP and Gas Absorption Heat Pumps (GAHP) also have the potential to materially reduce carbon emissions, and will in future offer consumers compelling financial benefits as technology costs fall. Given that GAHPs are recognised by the EU as renewable, we believe they should qualify for RHI payments in the UK to help bring forward the development of this technology.

**Question 7 - How can the Government incentivise the take-up of renewable heat technologies within a Green Deal successor scheme?**

The Green Deal proposition was based purely around financial savings, but renewable heat systems may reduce carbon emissions but not energy bills. Indeed, many renewable heat systems have very high up-front costs, and lead to only modest bill savings, making them poorly suited to pay-as-you-save schemes such as Green Deal Finance, where borrowing was constrained by the 'Golden Rule'.

Successful elements of the Green Deal scheme included those that provided grants, such as Cashback and the Home Improvement Fund. Neither of these schemes included renewable heat products, but if this approach was used in future, it could succeed in incentivising the take-up of these technologies.

Allowing 'assignment of rights' from schemes such as the Renewable Heat Incentive (RHI) also has the potential to help support the installation of renewable heat technologies. However, capitalising the RHI income would not be sufficient to cover the up-front installation costs, and so a significant contribution would be required from the consumer.