

# Inquiry Response

26<sup>th</sup> July 2019



## **Decarbonisation of the UK Economy and Green Finance inquiry**

The Energy and Utilities Alliance (EUA) provides a leading industry voice helping shape the future policy direction within the sector. Using its wealth of expertise and over 100 years of experience, it acts to further the best interests of its members and the wider community in working towards a sustainable, energy secure and efficient future. EUA has six organisational divisions - Utility Networks, the Heating and Hotwater Industry Council (HHIC), the Industrial & Commercial Energy Association (ICOM), the Hot Water Association (HWA), the Manufacturers' Association of Radiators and Convectors (MARC) and the Natural Gas Vehicles Network (NGV Network).

The Energy and Utilities Alliance (EUA) is a company limited by guarantee and registered in England. Company number: 10461234, VAT number: 254 3805 07, registered address: Camden House, 201 Warwick Road, Kenilworth, Warwickshire, CV8 1TH.

Given our position as a trade association, our comments on the inquiry's questions will relate primarily to the decarbonisation of heating and energy efficiency.

### **What economic costs and benefits does decarbonisation present for the UK?**

The cost of decarbonisation will be significant; it will require a substantial shift in energy production and usage, energy efficiency and usage as well as consumer behaviour and habits. These changes will be costly but the implications on cost and disruption of different strategies and technologies will vary greatly, underscoring the need for government regulation to guide the transition and ensure consumer and industry make the necessary changes.

However, decarbonisation will also provide the UK with many opportunities to become a world leader in the technologies that will enable our own transition to net zero carbon emissions by 2050. As we operate in the energy sector, our members are primarily concerned with the decarbonisation of space heating and hot water, both domestic and commercial. They are ready and able to be at the forefront of the transition to a decarbonised economy but they require certainty from the Government in terms of the fuels and technologies envisaged to be part of that transition in order to enable the necessary investments in development and infrastructure. If these decisions are made soon enough, the development of carbon neutral energy products, fuels and services could become a substantial asset for exporting abroad, something which is key to the Government's Industrial Strategy, as opposed to the alternative which would see us slip behind other economies which we become increasingly reliant on.

Decarbonisation will carry costs for consumers regardless of which technologies and/or fuels, if any, are favoured by the Government. A substantial increase in renewable electricity generation, and sufficient energy storage to flatten out spikes in demand and low levels of production, will have to be funded through bills or general taxation in order to meet increased demand. Similarly, significant investment will be needed to make nascent, but essential, technologies such as carbon capture, usage and storage commercially viable.

Within the heating industry, for example, certain technologies would carry a higher cost than others given the changes consumers would have to make to their homes and behaviours. For example, the Committee on Climate Change commissioned a study which estimated that in order to retrofit a heat pump in a typical British home, £26,300 would need to be spent which includes numerous potentially disruptive changes such as extensive insulation, larger radiators and installation of hot water storage if not already present<sup>1</sup>. The relative costs associated with the various technologies which could contribute to decarbonisation need to be factored in when appraisals are made of their respective costs and benefits to the economy and consumers.

We have an opportunity to become the world leader in the production of hydrogen and hydrogen heating products. The export potential of these products and expertise could soon be in very high demand as other economies around Europe and the world seek to decarbonise. Becoming a world leader in this field would be very much in line with the Government's commitment to developing high skilled jobs and the UK's status as an exporting nation as part of the Industrial Strategy. This cannot be said for many other forms of low carbon heating which we can already see are almost entirely imported with very little manufacturing or assembly taking place in Britain. Investment in a hydrogen economy could produce significant benefits, not only for the exchequer, but also for the wider economy and our efforts to meet the net zero 2050 target.

### **What benefits can a growth of the Green Finance sector deliver for the UK, and does the UK hold a competitive advantage in this space?**

The UK currently does not hold any competitive advantage in terms of green finance as this sector is underdeveloped compared with many other parts of the UK's financial sector. There needs to be a substantial growth in the availability and diversity of green financial products in order to support the transition to more energy efficient homes and low carbon heating systems. A key gap in energy policymaking in England has been the able-to-pay sector which has not been adequately incentivised to take up many affordable and widely available energy efficiency measures.

The obvious exception to this statement is the Government's former Green Deal scheme which was intended to provide homeowners with the opportunity to pay for a variety of measures, from new boilers and heating controls to insulation and double glazing, through savings made on their energy bills. This pay-as-you-save model, as well as the variety of measures on offer, were positive features of the scheme. However, any flexibility and freedom this offered to consumers was completely negated by the burdensome, bureaucratic application and assessment processes which householders were required to complete. The fact that repayments were tied to the property, rather than the initial borrower, which in many cases caused issues with lending and the selling of homes. When measures did not deliver the savings on energy bills predicted at the point of assessment, some homeowners have become trapped by repayments which are far higher than they were lead to believe they would be. This kind of green finance puts many householders who might otherwise be interested in investing in energy-related home improvements and also undermines public confidence in the sector and the wider energy industry.

---

<sup>1</sup> [UK Housing: Fit for the future?](#), page 42, Committee on Climate Change, February 2019

The UK ought to be able to leverage its leading position in the global financial sector to deliver affordable, flexible and convenient green finance options to homeowners and landlords. By the nature of many measures, including new central heating systems, consumers are faced with high upfront costs which in many cases they are unable to meet, despite them knowing that they could lead to significant savings in the long run. The Treasury should learn lessons from the Scottish Government's *Home Energy Efficiency Programmes for Scotland* which brings together a number of different schemes, each aimed at a different segment of the housing market, from social landlords to able-to-pay households as well as fuel poor homeowners and private sector tenants<sup>2</sup>. These schemes are led by the independent Energy Savings Trust which guides applicants through the process and, in the case of able-to-pay households for example, provides them with access to hassle-free, low cost finance.

If we are able to ensure that green finance is widely accessible, well-advertised and carrying as little bureaucracy for individuals as possible, then it would become a vital component of the transition to a decarbonised economy. Currently, households have little incentive or choices when it comes to upgrading the energy efficiency of their heating systems and homes. Therefore, without a vast increase in the availability of green finance, we will not be able to achieve our targets in reducing domestic carbon emissions.

### **How might HMT deliver a regionally balanced and 'just' transition across the UK?**

Within its strategies to enable the transition, the Treasury must recognise that different parts of the UK face varying challenges when it comes to energy. For example, many rural areas which are not connected to the gas grid suffer from high levels of fuel poverty. These areas will require a very different approach to more urban areas which benefit from a gas grid connection. Treasury-funded schemes to alleviate fuel poverty will need to take account of particular difficulties in certain regions.

The Treasury should also recognise that the way in which the transition is funded will be key to whether it can be regionally balanced or considered 'just'. As previously mentioned, Scotland's energy efficiency schemes are well developed and this is true, albeit to a lesser extent, for Wales. This leaves consumers in England and Northern Ireland with relatively few options for accessing funding or finance for energy efficiency improvements, particularly ones which give them a wide degree of choice. If this situation is not rectified by the Government providing a better offer and more encouragement of green finance, then any transition which comes will not be regionally balanced by virtue of a postcode lottery for energy consumers. Furthermore, if the focus remains on consumers either funding their own part of the transition, or putting system-wide costs onto energy bills which are regressive by nature, then it cannot be a just transition. Those who are least able to pay need to be assisted in making the transition to decarbonised heating with a parallel aim of reducing their energy bills which will impact them disproportionately compared to wealthy households.

### **What is HMT's current strategy, and approach to, UK decarbonisation, and is it fit for purpose?**

The Treasury's current strategy towards the decarbonisation of heat is to fund individual, specific subsidy schemes such as the Renewable Heat Incentive (RHI) and, until recently, the Feed-in Tariff

---

<sup>2</sup> [Home energy and fuel poverty](#), Scottish Government

Scheme (FiTS). These schemes have funded low carbon heating systems but do not have the reach needed to support the widespread transition that we need to see. Developing a truly mass market for energy efficiency products and facilitating the development of new low carbon heating options, such as hydrogen, should be central to the Treasury's decarbonisation strategy but so far the funding for projects and schemes which could drive these aims has not always been provided.

If our 2050 net zero target is to be achieved, the scope of schemes for domestic heating will need widen considerably from currently inadequately low levels. For example, since its inception in April 2014, the RHI has only delivered 45,126 new heat pumps, biomass boilers and solar thermal systems<sup>3</sup> against a total expenditure on subsidy payments of £396 million<sup>4</sup>. Compare this to the number of inefficient gas boilers, rated F or G, still in British homes which is estimated to be around three million. A boiler scrappage scheme aimed at replacing these so-called 'zombie boilers' with modern, efficient A-rated models would not only provide significant savings on energy bills to the households affected, it would also stimulate demand for other products associated with heating systems and energy efficiency, not to mention wider benefits around efficient use of gas and improvements to air quality. This single example of how subsidies are currently used and how they potentially could be used underscores the fact that the Treasury is primarily concerned with incentivising a small number of transitions amongst primarily wealthy owner-occupiers which will not achieve the level of market penetration needed to facilitate a nationwide reduction in domestic emissions.

### **How does HMT work with the Clean Growth Strategy and government departments to support decarbonisation? Is this working well?**

The Treasury is the chief funder of policies which stem from the Clean Growth Strategy so the level of ambition and reach of these approaches is determined by its level of support. In some cases, the decision to curtail or restrict schemes, such as the RHI and FiTS, has essentially been taken by the Treasury as they have restricted the amount of funding allocated to them. In this way, the Treasury can limit the scope of schemes which their respective departments may wish were more ambitious. Often departments wait to see the level of financial support the Treasury is willing to commit before they put forward any proposals. To some extent, this will always be the case but recent announcements in the Chancellor's Spring Statement around standards for new build properties and decarbonising the gas grid show that the Treasury can sometimes even unexpectedly take the lead on policy announcements with departments then expected to work out the detail.

We would prefer for the Treasury to take a longer term view of supporting decarbonisation. Currently, many schemes are being funded on a year-to-year basis and the flagship subsidy scheme for low carbon heating, the RHI, was due to end in 2020. Any decision making around a successor scheme has been delayed and its funding extended until 2021. A lack of clarity around what might follow the RHI, to what extent it might be funded by the Treasury, its scope and target consumers, the technologies it might cover, etc. is creating a degree of uncertainty within the heating industry which, coupled with uncertainty around Britain's exit from the European Union, means there is currently a unfavourable environment for investments.

---

<sup>3</sup> [RHI deployment data – June 2019](#), Department of Business, Energy and Industrial Strategy

<sup>4</sup> [Public reports and data: Domestic RHI](#), Ofgem

The Department for Business, Energy and Industrial Strategy is looking to develop a long term roadmap for heat policy, something which would be welcomed by many of our members, but again timescales on this are uncertain because the Department is still awaiting an indication from the Treasury on how much funding it will commit to heat decarbonisation in the coming years. The Treasury could do a lot more to enable these kinds of vital decisions to be made and support other departments in taking forward their plans to deliver decarbonisation.

### **How should HMT's approach evolve to ensure the Government meets the legally binding carbon budgets (and the net-zero targets, if applicable)?**

The way in which the Treasury funds and facilitates decarbonisation will need to be flexible as new technologies and challenges emerge. The Government's overall strategy will need to be adaptable for any transition to be successful, particularly if we are to achieve net zero by 2050. A rigid approach from the Treasury could choke off development of new innovations and approaches to our energy system. The Treasury should avoid 'picking winners' by maintaining a broad approach to technologies and fuels which can deliver decarbonisation. This will enable transitions to happen differently in different parts of the country and allow for new technologies to enter the market even whilst the overall goals and strategies for decarbonisation remains the same.

### **What role should the 2019 Comprehensive Spending Review play in UK decarbonisation? What projects or measures should receive additional funds through this process?**

We believe that the Comprehensive Spending Review is an opportunity for the Treasury to recognise that the long term transition of heat needs to begin now. Schemes such as the RHI have not delivered the scale of change needed so the CSR will need to provide certainty to BEIS that there will be sufficient funding for their long term heat decarbonisation strategy to be delivered. We believe that progress on demonstrating the viability of hydrogen as a zero carbon fuel for Britain's gas grid needs to be a key focus for the Government going forward. Therefore, the Treasury will need to make this a core part of the pledge made in the Spring Statement around the greening of the gas grid; clearly this will need to be back up by funding and credible policies development in close co-operation with BEIS.

We also feel that the Treasury needs to place a greater emphasis on incentivising a wider range of households to invest in improvements to their heating system and their home's energy efficiency. As previously mentioned, this is something which has been lacking since the failure of the Green Deal but is available to households in Scotland.

### **What role do UK financial services firms currently play in the decarbonisation of the economy, (for example, through stewardship, capital allocation to green projects, green financial products)? What more can they do?**

Loans are available to householders for improvements to their home but they are often not affordable given the long payback times for many heating system and energy efficiency products. More explicitly energy-focused financial products, such as green mortgages, have been mooted but it remains difficult for the able-to-pay sector to access finance which is low cost and low risk whilst also meeting the high upfront costs of many measures covered by Scotland's HEEPS

schemes. Currently, there is no greater incentive to borrow for a more efficient heating system or an energy efficiency measure than for an extension or home renovation project which is a key barrier to driving uptake of these measures.

If the Government provided more guidance and a regulatory framework around green finance products then they could become more established and popular among consumers.

### **What is the consumer demand for 'green' financial products?**

Demand for green finance is currently very low due to a general lack of awareness amongst consumers and a lack of Government guidance. Returning to the example of Scotland, their energy loan and grants schemes are administered and fronted by the Energy Savings Trust who are clear in their offer of free energy advice for all, such as a free, personalised home energy check. Most awareness of green finance in England is negative as it has been driven by the poor experience of the Green Deal and the continuing fallout and resultant negative headlines that it generates. There are also concerns around how mandating products such as green mortgages could restrict house sales amongst vulnerable homeowners who do not have the means to upgrade the energy efficiency of their property.

### **Are there a range of accessible options available to consumers seeking to source 'green' financial products across the product suite (for example, mortgages, bonds, investment products, savings accounts, loans)? Do certain instruments dominate the green finance landscape, and if so, why?**

No, choice is currently very limited. For example, loans for energy-related improvements are typically not treated any differently to loans for any other home improvement. The Government's Green Finance Strategy may go some way to addressing this but this will take time to have any kind of impact on the sector.