

Energy Efficient Scotland Owner Occupied Proposals

A BSA Response

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 Building Societies
Association

Introduction

The Building Societies Association (BSA) represents all 43 UK building societies, as well as 6 credit unions. Building societies have total assets of £420 billion and, together with their subsidiaries, hold residential mortgages over £330 billion, 23% of the total outstanding in the UK. They hold over £290 billion of retail deposits, accounting for 19% of all such deposits in the UK. Building societies account for 38% of all cash ISA balances. They employ approximately 42,500 full and part-time staff and operate through approximately 1,470 branches.

We have responded below to only the questions where the BSA and our members have particular experience or expertise.

Responses to questions

1. Do you agree or disagree that there should be a legally-binding energy efficiency standard for owner-occupied housing?

The BSA agrees with the intent of the proposal. However we have significant concerns about the proposed method of implementation and the negative effects this could have on the Scottish housing market. We would argue that the Government should instead pursue a phased implementation which will give consumers a timeline over which to incrementally improve their property, rather than a single date beyond which they might be faced with a large capital bill.

2. Do you agree or disagree that EPC Energy Efficiency Rating band C is the appropriate standard to use?

An initial standard of EPC Band C risks overwhelming retrofit supply chains and bringing the housing market to a standstill as homeowners wait for works to be carried out before they can sell.

Instead the Government should pursue a phased approach, focusing on the least energy efficient homes first. This will enable the industry to create financial products to fund improvements and for the retrofit supply chain to gear up and learn lessons around implementation of a more ambitious standard.

3. What are your views on the “fabric first” approach?

The BSA agrees that "Fabric first" is the correct approach. The Government should consider whether the obligation should focus entirely on the fabric of buildings in the first instance as supply chains are relatively more mature in this area than the low-carbon energy sector.

Requiring homeowners to install a heat pump before the fabric of the building is optimised could lead to poor consumer outcomes as the technology may not function as specified. There will also be a significant number of homes in more remote and rural

locations which will not have access to district heating, even if the network is vastly grown on current numbers.

Focusing on the fabric of the buildings in the first instance will also help homeowners to spread the cost into phases, rather than the entire cost of bringing a home up to EPC Band C being triggered by a single sale.

4. In your view, how can we ensure that when EPCs are used to determine compliance with the standard, they are robust and not easily open to misuse?

No comments.

5. Do you think the standard should be fixed, or should it be subject to periodic review and change over time?

The BSA believes the standard should be phased in and subject to periodic reviews to grow the supply chain and learn lessons over time.

6. Do you agree or disagree that 2024 is the right start date for the mandatory standard to start operating?

2024 gives a fair window of notice for homeowners to become aware of the standard. We agree that commencing phasing in of standards should begin earlier than 2030 and 2024 appears sensible. However, we caution against mandating EPC Band C in 2024 as this could have serious negative consequences for the Scottish housing market. Government should consider a phased approach.

7. Do you agree or disagree with point of sale as an appropriate trigger point for a property to meet the legally-binding standard?

This would appear to be a sensible trigger point.

8. Do you agree or disagree that responsibility for meeting the standard should pass to the buyer if the standard is not already met at point of sale, as described above?

There needs to be careful consideration of how this would work in practice. The buyer would need to have visibility of any costs of meeting the standard before committing to the purchase. Government should consider how this information can be standardised and passed to the buyer up-front.

This measure will also have an implication on the mortgage valuation as the valuer is required to take any known capital costs into account that will fall on the buyer. This is likely to lead to 'down valuations' on energy inefficient homes which could reduce their saleability and marketability.

Similarly, these costs will need to be taken into account by mortgage lenders in their affordability assessments. Where a buyer is able to meet the costs out of their own savings this might be acceptable. However, if they would need to take on additional credit beyond what the mortgage lender is able to provide, this could lead to the mortgage being

turned down. This will particularly be an issue for first-time buyers who tend to have higher loan-to-value mortgages.

9. What, if any, unintended consequences do you think could happen as a result of these proposals? For example, any positive or negative effects on the house sales market.

The BSA is supportive of the principal of these proposals. A clear positive effect will be making the energy performance of a home a much more prominent driver in people's decisions on which home to buy. This in turn should help to grow the supply chain for retrofit works and increase demand for energy efficient homes.

Unfortunately we can also foresee significant negative effects on the house sales market.

Firstly, there is a risk of 'stranded assets' with homes where it is not technically feasible to retrofit the fabric of the home with the result that in extreme cases these may need to be demolished and rebuilt unless there are appropriate exemptions.

Secondly, if a homeowner cannot afford to carry out the works needed to bring the home up to a C, and cannot find a willing buyer then there is a risk of people being stuck in a home they are unable to sell.

Thirdly, as stated above, the proposals could have a disproportionate effect on first-time buyers who tend to borrow at higher loan-to-values.

Finally, we can see a risk of negative equity. For example, if a borrower has a high loan-to-value mortgage when the proposals come in, their equity will in theory be eroded by the cost of the works from day one. Should they fall into payment difficulty and the lender is required to repossess then the borrower could owe more than the home is worth pre-works, unless there is an exemption from the proposals for a mortgagee in possession. There is a question whether lenders will also need to hold more capital against such loans, making it more expensive to lend and potentially leading to a lack of finance for energy inefficient homes.

10. Do you agree or disagree with point of major renovation as an appropriate trigger point for a property to meet the legally-binding standard?

This would appear sensible so that costs do not all crystallise at the point of sale.

11. What is your view on how "major renovation" should be defined? Should the Energy Performance of Buildings Directive definition, as described in Annex B, be used?

In the BSA's view, the major point to consider is whether the "major renovation" will be affordable taking the required consequential works into account. People may fund a renovation from savings but are more likely to take a further advance on their mortgage. If the borrower is already borrowing a significant amount of their equity, they may not be able to borrow more to cover the full cost of energy efficiency improvements.

Government should consider whether there is a list of works that can be provided with some benchmark costs attached. People might then be required to carry out a few of the

more immediate works during the renovation, while being able to spread the cost with carrying out the rest prior to sale.

Therefore, an option for Government is to set the bar for "major renovation" lower than 25% of the value of the building, as this would mean people carry out works more often but do not suddenly get hit with a large extra capital cost.

Admittedly, the BSA would need clarity from the Government on how it intends to exclude the value of the land from the equation as land is an integral part of the value of any home.

12. How could a requirement to meet the energy efficiency standard at point of major renovation be checked and enforced?

This would likely need to involve EPC assessors working with local building inspectors. It would only need to be enforced at point of sale, likely by the conveyancer.

Who should be responsible for this?

The responsibility will fall on the homeowner to check whether they meet the standard at the point of sale. It is immaterial whether this is done in one stage or over a number of renovations.

15. At what level, approximately, should any penalty be set?

We believe that the Land and Buildings Transaction Tax framework could be amended to provide incentives and penalties. For example, where someone fails to meet the standard, they could be subject to an LBTT surcharge on their next property purchase. Payment of the surcharge could be arranged through the conveyancing process. This would reduce the risk of stranded assets that would arise if Government were to make it illegal to sell a home that does not meet the standard.

28. In your view, what are the most important considerations for homeowners who are required to meet the legally-binding standard, in relation to skills, supply chain, consumer protection and quality assurance?

Quality assurance and consumer protection are absolutely paramount in order to build confidence in the energy efficiency retrofit industry. Energy efficiency improvements should be seen as a means of adding value to the property, not a risk of damaging it. Therefore a strong redress scheme with only approved retrofit providers legally allowed to carry out energy efficiency improvements should be established. In order to become approved, a provider should have to be part of the redress scheme, which could be overseen by a Retrofit Ombudsman. This should be a far more streamlined and specialist route for getting compensation, rather than having to pursue tradespeople through court.

31. Do you agree or disagree that grant funding from the public purse should be focused on households who are vulnerable or in fuel poverty? Please explain if you disagree.

We agree that vulnerable and fuel poor households should be the focus of Government grant funding. However, Government should also consider whether they can assist in situations where a homeowner is able to pay for some improvements but the overall cost of the retrofit outweighs any possibility of payback. We are thinking particularly of households in very hard to treat properties.

32. In your opinion, what sources of non-government, private sector support are people most likely to want to access? (eg from banks, building societies, credit unions, mortgage providers)

The Building Societies Association has convened a Green Finance Taskforce to look at the issues around creating a market for green mortgages and other finance products. The Taskforce includes representatives from over 20 societies, with a mix of Chief Executives, Chief Product Officers, Chief Risk Officers, Heads of Distribution and others from across the business.

Through the course of the Taskforce's work so far we have identified the need to develop the market in three main areas: Education, Proposition and Communication. Education is particularly focussed on what information consumers need from their lender, the Government or from other sources to feel confident in researching and ultimately commissioning energy efficiency improvements to the property.

Proposition looks at what kinds of products will incentivise customers to green their home. This could take a number of forms, such as a rate incentive on their mortgage, equity loans, preferential affordability assessments or cashback on the mortgage to carry out certain improvements.

Finally, communication focuses on what is needed from wider stakeholders to support a market for green finance products, whether through regulatory definitions, distribution through brokers or support from the Bank of England or Government through the tax system.

In our view, there is scope for a range of financial solutions depending on the kind of improvement a borrower wishes to carry out. For example, installing a more efficient boiler might be suitable to unsecured lending, whereas an improvement to the structure of the property such as installing triple glazing or insulating walls may be more suited to secured lending through a further mortgage advance.

We would welcome further dialogue with Government as the BSA's work on green finance develops going forward.

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The Building Societies Association (BSA) is the voice of the UK's building societies and also represents a number of credit unions.

We fulfil two key roles. We provide our members with information to help them run their businesses. We also represent their interests to audiences including the Financial Conduct Authority, Prudential Regulation Authority and other regulators, the Government and Parliament, the Bank of England, the media and other opinion formers, and the general public.

Our members have total assets of over £420 billion, and account for 23% of the UK mortgage market and 19% of the UK savings market.