

HM Treasury Consultation: Economic Instruments To Improve Household Energy Efficiency

Response by the UK Business Council for Sustainable Energy

1 INTRODUCTION

- 1.1 The UK Business Council for Sustainable Energy (UKBCSE, the Council) includes Innogy, BP, Shell UK, Powergen, National Grid Transco plc, United Utilities and Scottish Power. It has been created in order to develop an effective dialogue with Government that can help strengthen the UK's strategic agenda for sustainable energy.
- 1.2 These major businesses all have an interest in renewables, energy efficiency and CHP and the UKBCSE is working to build a broad consensus on many of the issues surrounding the development of sustainable energy in the UK.
- 1.3 The Council welcomes the Treasury's consultation coming as it does at a crucial time in the Government's energy policy review process and the recognition it gives to the role of energy efficiency in developing a sustainable energy system.
- 1.4 In the long term the Council believes that some form of carbon pricing and ultimately carbon trading should be introduced more fully into the energy market to better reflect the environmental impact of carbon emissions from energy production and use. This would allow for carbon reductions to be made where it is most cost effective to do so and provide an incentive for suppliers and consumers to develop sustainable energy technologies.
- 1.5 However, the Council accepts that this mechanism on its own, at least in the short term, will not be enough to drive the development of sustainable energy and that a mix of instruments – policy, regulation and economic – will be needed to fully exploit the benefits of sustainable energy.

2 IMPROVING HOUSEHOLD ENERGY EFFICIENCY

- 2.1 The Council believes that energy efficiency is currently one of the most cost-effective methods of reducing emissions but that there are numerous barriers to the take-up of the measures that will deliver the reductions in energy use identified as possible.
- 2.2 The Council agrees with the Treasury (and others) analysis of the barriers to the greater uptake of energy efficiency in the domestic sector. In particular the Council believes that one of the biggest barriers to the uptake of energy efficiency measures in the domestic sector is the fact that energy costs are a very small proportion of overall household income. This gives no financial incentive for consumers to reduce their consumption further and also means that any move to increase energy prices will, on its own, have no real impact on energy consumption unless levied at an extremely high, and unrealistic, level.
- 2.3 The Council therefore supports the need for additional measures in the domestic sector including economic instruments. Other measures will also be needed, particularly changes to the Energy Efficiency Commitment (EEC) mechanism and fuel poverty programmes. The Council believes that the end of the current programme in 2005 should be used as an opportunity to modify the EEC towards a more tradable instrument.
- 2.4 The Council believes that the three economic measures that would be of the most benefit are: extension of reduced VAT rates to other energy efficiency products (and increased taxes for inefficient products); tax credits for implementing energy efficiency measures; stamp duty (or similar) rebates for energy efficiency improvements at the time of house purchase.

Reduced VAT Rates

- 2.5 The Council believes there is a case for extending the 5% VAT rate to other energy efficiency products and is aware of the calls for this reduced rate to be applied to products such as A-rated appliances, condensing boilers, micro-CHP, Community Energy networks, compact fluorescent light bulbs, solar installations etc. Reducing the VAT on these, and other energy efficient products will be of benefit both in terms of incentivising householders directly in their purchases and guiding installers towards the most efficient products.
- 2.6 However, the Council believes that there does need to be a more standardised and simple method of identifying which products should attract this lower level of VAT. There are currently numerous different mechanisms for identifying qualifying 'energy efficient' or 'low carbon' products – e.g. the Energy Saving Trusts 'Energy Efficiency Recommended' scheme; DEFRA's CHPQA scheme, the Enhanced Capital Allowance (ECA) scheme of the Climate Change Levy package – and some kind of standardisation, based on carbon or energy efficiency would be useful.
- 2.7 A corresponding and supporting measure that would strengthen the reduction in VAT for energy efficient products would be to increase the tax rate on the most inefficient

products, such as incandescent light bulbs, non A rated appliances etc. The Treasury have already set a precedent for this type of measure through the Climate Change Levy which is levied on the price of electricity but not on renewable or CHP based generation due to their environmental benefits.

- 2.8 The introduction of 'across-the-board' VAT reductions for energy efficient equipment etc. (and the complementary tax rise on inefficient equipment) would present the opportunity for industry - energy suppliers, installers etc - to embark on a mass advertising programme to boost take-up beyond that would happen from the tax changes in isolation. It is therefore imperative that any such changes are planned with industry to ensure the full benefits are realised.

Tax Credits

- 2.9 Allowing householders to offset expenditure on specific energy efficient installations against, for example, their Income Tax bill or Council Tax bill will give an additional incentive to householders. Offsetting expenditure against personal Income Tax will only be possible where a householder undertake self-assessment, but allowing for a reduction in Council Tax as a result of implementing specific measures could be more universally applied.
- 2.10 Some form of tax credits scheme could also be used to incentivise landlords to improve their rented properties - currently one of the most difficult areas of the sector to address. Allowing landlords to claim energy efficiency improvements as a business expense - and claim a tax allowance for the investment - would encourage them (or at least would not act as a dis-incentive) to make improvements to their properties. To do this however would require a change to the current tax allowance definitions - and allow energy efficiency installation to class as 'replacement' rather than 'betterment' - as has been done for double glazing.
- 2.11 As with the reducing VAT rates proposal outlined above there needs to be a standardised measure of what classes as a 'qualifying energy efficient investment.'

Stamp Duty Rebates

- 2.12 The Council also believes that it is when a person moves house that there is the best opportunity to undertake energy efficiency improvements and that house purchasers could be better incentivised to undertake such improvements.
- 2.13 The Council believes that energy audits should become a requirement of the overall house condition survey carried out as part of the house purchase process (as currently exists in the draft EU Building Directive). This will allow house purchasers to identify the actions that could be taken to improve the efficiency of the housing stock. These actions could be rewarded through a reduction in the stamp duty paid on the purchase and could form the basis for a preferential mortgage rate.

3 CONCLUSION

- 3.1 The UK Business Council for Sustainable Energy believes that there is a need for new and additional measures to improve the up take of energy efficiency measures in the domestic sector. These measures include policy, regulation and economic instruments which will all be necessary to address some of the identified barriers. In addition there must be a move, in the longer term, towards carbon pricing and carbon trading to allow for measures to be introduced where they are most cost effective.

October 2002

The views expressed in this paper cannot be taken to represent the views of all parts of all the companies in the UK BCSE. However, they do reflect a general consensus.