Committee on Climate Change

The Rt Hon Chris Huhne MP

Secretary of State

Department of Energy and Climate Change

20 December 2011

Dear Chris

Proposals for the Green Deal / Energy Company Obligation

I am writing to you to express the concern of the Committee on Climate Change about some of the detailed proposals for the Green Deal and the Energy Company Obligation (ECO).

In particular, DECC's draft Impact Assessment notes that loft and cavity wall insulation account for much of the cost effective potential to improve energy efficiency in the residential sector, but projects that implementation of these measures will be very limited under the proposed policy approach. This is consistent with our own assessment, as set out in our third progress report to Parliament.

Low uptake would be problematic given the need to insulate lofts and cavity walls to meet carbon budgets, and to mitigate energy bill impacts from investment in low carbon power generation.

There has been good progress insulating lofts and cavity walls under the current Carbon Emissions Reduction Target (CERT) policy. We therefore propose that the new policy should build on this, and that DECC / the Government should seriously consider including full potential for loft and cavity wall insulation in the ECO.

The result would be a level of policy ambition that addresses much more of the potential for emissions reduction than the low level likely under the current proposal (e.g. 4-5 $MtCO_2$ in 2020 rather than 2 $MtCO_2$), while still achieving other policy objectives to contain funding costs and develop new markets for energy efficiency.

More details are included in an attachment to this letter.

We are putting the letter in the public domain to promote debate and discussion in a crucial area for achievement of carbon budgets and mitigating energy bill impacts.

Yours ever

Adair Turner, Chair, Committee on Climate Change

cc. Greg Barker, Minister for Energy and Climate Change

The Committee on Climate Change
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Attachment: the need to increase loft and cavity wall insulation under the Green Deal and the Energy Company Obligation

Strengths in the proposed approach: solid walls, the non-residential sector

Proposals for the Green Deal and the Energy Company Obligation (ECO) include a range of innovative approaches (e.g. provision of information, accreditation of suppliers, brokering arrangements to support development of new markets for energy efficiency in conjunction with the ECO, a new financing instrument, regulation of the private rented sector, and performance monitoring).

These could encourage uptake of solid wall insulation in the residential sector, energy efficiency improvement in the non-residential sector, and could provide needed support for fuel poor households.

Low ambition for loft and cavity wall insulation

However, the draft Impact Assessment (IA) suggests that the Green Deal and ECO are only expected to address around 2 $MtCO_2$ of the 5 $MtCO_2$ cost effective potential for energy efficiency improvement through building fabric measures in the residential sector.

The difference between cost effective potential and expected policy delivery relates largely to projected low levels of investment in loft and cavity wall insulation:

- The IA notes success on loft and cavity wall insulation under CERT, and attributes this to the subsidy under this policy.
- It identifies expected remaining potential from 2013 to top up 6 million lofts, and to insulate 6.3 million cavity walls. There could be additional potential depending on performance of CERT in the second half of 2011 and in 2012 (i.e. if CERT targets are not achieved).
- It suggests that the Green Deal, together with baseline uptake, will only result in insulation of 700,000 lofts (around 10% of potential) and 1.7 million cavity walls (around 30% of potential – and only 15% of the rate achieved under CERT).
- It rules out delivery of lofts and cavity walls under ECO, reflecting the proposed policy design, and an assumption that inclusion of these measures in ECO would incur deadweight costs.

The projected low levels of uptake relative to potential are similar to what we envisage under a market-based approach (i.e. through the Green Deal rather than the ECO), given significant non-financial barriers to uptake, and as set out in our third progress report to Parliament.

Implications of low ambition for carbon budgets and energy affordability

Low uptake would be problematic from a carbon budget perspective for two reasons:

- Both our emissions projections and those of DECC for meeting the first four carbon budgets assume that all lofts and cavity walls are insulated over the next decade (e.g. the Carbon Plan states the aim to maintain installation rates for loft and cavity wall insulation at today's levels over the next decade)

- Insulation of lofts and cavity walls is required to support the roll-out of renewable heat in the residential sector during the 2020s. A less energy efficient housing stock would raise costs and risks of investing in renewable heat. The reason for this is that electric heat pumps (the most promising option for the residential sector) work less efficiently in houses which are not well insulated, and because such houses require more heat.

It would also be problematic from an affordability perspective, where loft and cavity wall insulation offer opportunities to partially offset the impact of projected increases in energy prices over the next decade.

In addition, the current proposal represents an inefficient way of spending ECO funding. A more efficient way would be to use ECO funding to support solid wall insulation, together with loft and cavity wall insulation where required. In this case there would be greater emissions savings and energy bill reductions for a given amount of funding.

Complementing the Green Deal by increasing ECO ambition

A higher level of ECO ambition would complement rather than crowd out Green Deal finance, and would be consistent with such finance being provided by a range of delivery partners:

- We do not accept the argument in the IA that including loft and cavity wall insulation in the ECO would crowd out the Green Deal finance, particularly given that the IA suggests limited uptake under the latter approach.
- More importantly, we believe that inclusion in the ECO would be compatible with 100% Green Deal finance in some cases and blended financing in others (i.e. a

combination of Green Deal finance and ECO funding); it would not imply the need for 100% subsidy of loft and cavity wall insulation.

- It would also be compatible with delivery by a full range of partners under the proposed brokering arrangements, just as solid wall insulation under the ECO could be delivered under these arrangements. In fact, given more ambitious targets, wider participation in delivery may be required in order that these are achieved.

Inclusion in the ECO would therefore underpin the proposed approach and provide confidence that insulation of lofts and cavity walls will actually ensue.

Scope for increased ambition at current funding levels

A high level assessment suggests that there would be scope for delivery of loft, cavity and solid wall insulation required to meet carbon budgets within the current ECO funding envelope (i.e. around £1.3 billion annually) if energy companies and Green Deal providers were sufficiently incentivised to control costs.

This could be achieved through the use of blended financing, together with detailed policy design to minimise costs (e.g. a focus on internal solid wall insulation, exploiting potential for scale economies through area based approaches, measures to reduce or limit the impact of hidden costs including possible regulation and fiscal incentives).

Recommendation on the Green Deal and ECO

Given the importance of achieving high rates of loft and cavity wall insulation over the next decade, but the low levels of likely delivery under the approach proposed in the consultation document, we recommend that DECC / the Government strengthens the new policy by including potential for all loft and cavity wall insulation in the ECO (i.e. ambition should be set at 4-5 $MtCO_2$ in 2020 than your proposed 2 $MtCO_2$), and urge the department to carry out a full assessment of this option.