Ecology Building Society response to the Call for Evidence on Building a Market for Energy Efficiency

Introduction

Ecology Building Society was established in 1981 to help finance environmental building, renovations and support sustainable development. Since then we have broadened the reach of our lending but throughout we remain dedicated to supporting projects that have a positive impact on the environment and improve the quality of housing across the UK.

Ecology is widely recognised as a sustainable finance pioneer and leading 'green mortgage' provider in the UK. We specialise in lending for ecological new builds (including self-build and custom build), renovation or conversion of derelict buildings, and energy efficiency improvements to existing buildings. We also lend to community owned businesses, affordable housing including shared ownership and community-led housing, organic smallholdings and to enable low-impact sustainable lifestyles, such as moorings for houseboats.

In 2016 (the latest period available) we provided £30.7 million of lending across 120 sustainable properties and projects throughout the UK. This included supporting 23 renovations (typically whole house retrofit) and 9 conversions of non-residential property to residential.

Improving the energy efficiency of our existing housing stock will be critical to help meet our carbon targets, and while we welcomed the ambition set out in the Clean Growth Strategy to improve as many homes as practical to EPC band C by 2035, we recognise the need for practical policies that will deliver. Through our range of 'C-Change' mortgage discounts we already incorporate energy efficiency into our lending decisions and pricing. The call for evidence acknowledges that there is no 'silver bullet' to increase the take-up of home energy efficiency measures and it is clear that a range of policy interventions will be required. As an existing provider of green mortgages for renovation and retrofit, we are ready to work with policy makers and other stakeholders to share our knowledge and experience to help deliver on this ambition.

Our C-Change mortgage discounts

We want to incentivise people to build, buy or renovate sustainably so we reward borrowers whose properties are more energy efficient (therefore have lower carbon emissions) with our range of 'C-Change' discounts off our Standard Variable Rate (SVR) which helps them reduce their mortgage repayments for the duration of their mortgage term. The level of discount is based on the homes' energy performance.

We offer three types of discount:

- C-Change sustainable homes

Our C-Change sustainable homes discounts reward people who build or purchase an energy efficient home, or who undertake a comprehensive eco-renovation of an existing property to Passivhaus EnerPHit standard.

The tables below explain our levels of discount and the standards they relate to. The first table deals with a range of energy efficiency standards, while the second table details our special discounts for Passivhaus related standards.

General standards		
Discount level	**Discount %**	**Standards**
1	0.50	EcoHomes Very Good EPC B
2	0.75	EcoHomes Excellent EPC A AECB Silver (Carbonlite Step 1) CSH Code Level 4
3	1.00	CSH Code Level 5
4	1.25	CSH Code Level 6 AECB Gold (Carbonlite step 2)

Passivhaus standards		
Discount level	**Discount %**	**Standards**
2	0.75	EnerPHit (PHPP modelled)
4	1.25	Passivhaus EnerPHit EnerPHit[+i]

CSH = Code for Sustainable Homes
EPC = Energy Performance Certificate
AECB = the sustainable building association
PHPP = Passivhaus Planning Package

- C-Change retrofit

Our C-Change retrofit discounts are designed for any existing home requiring extensive improvements. A discount of 0.25% from our SVR is available for each EPC grade improvement in either the energy efficiency or environmental improvement rating. For example, if either rating improves from F to C after the improvement works are completed, a discount of 0.75% will be available on the whole of the mortgage for the duration of the loan following certification of the improvements.

- C-Change energy improvements.

This gives a 1.00% discount from our SVR on mortgages for specified energy saving or renewable energy systems. The range of measures which qualify for the discount include installing insulation, double or triple glazing, a condensing boiler, wind turbines, photovoltaics, solar water heating, biomass heating, ground source heat pumps, heat recovery systems, installing low water-use appliances (e.g. low flush toilets) and rain water harvesting.

Responses to Questions (where applicable)

State of the market

3. Do you agree with our assessment of the current market for energy efficiency amongst owner occupiers, including the trigger points and supply chain relationships?

We broadly agree with the assessment set out of the current market for energy efficiency amongst owner occupiers.

Our experience is that our borrowers often undertake energy efficiency improvements as part of other extensive construction works. For example these improvements may form a key part of an environmental new build or a renovation or conversion of an existing property - a ‘whole home retrofit’. It is therefore important to recognise the importance of developing policies that support a multi-skilled supply chain that is able to deliver both innovative and effective energy efficiency improvements alongside other building improvements.

4. Do you agree that it makes sense to prioritise those groups most likely to be open to investing in energy efficiency? And do you agree with our assessment of who those groups are most likely to be?

While it does make sense to initially prioritise those groups, particularly early adopters, who will be most likely to be open to investing in energy efficiency, we also believe that, given the ambitious installation rates which will be required to move all English properties up to EPC band C and support the delivery of the UK's climate change commitments, consideration needs to be given to policies which will support the whole of the market.

Proposed approach

10. Do you agree with the set of proposed principles for guiding our approach?

The principles set out in the call for evidence seem logical. However in addition consideration should be given to policies which will support the whole of the market for owner occupiers if we are to build the scale of energy efficiency improvement interventions which will be required to support the delivery of the UK's climate change commitments.

11. Do you agree that the policy areas we have set out are the correct ones?

We broadly agree with the policy areas set out in the call for evidence. As a lender which specialises in providing mortgages for environmental building projects we would consider the development of new methods for financing energy efficiency to be a 'supply side measure' rather than the 'demand side measure' outlined in the call for evidence.

Developing new ways for financing energy efficiency

12. Which of the fiscal levers described here would drive the greatest consumer demand?

As discussed in the response to Q11 we would consider the fiscal levers outlined in the call for evidence to be key to improving the supply of energy efficiency improvements.

Ecology's lending is focused on first charge mortgages, which are secured on the value of the property. We do not currently offer unsecured loans or, second charge or conditional mortgages. In practice we believe that the challenge of improving the energy efficiency of the UK's housing stock will require a combination of the multiple levers outlined in the call for evidence as well as considering the role of first charge mortgages.

13. Is there evidence to suggest that any other fiscal levers not described here could drive consumer demand?

The role of first charge mortgages such as those provided by Ecology should also be considered. This might be particularly applicable where a mortgage is required to purchase and then renovate a property, including where the borrower requires mortgage funding in staged releases as the work progresses and the value of the property increases.

16. What barriers, regulatory or otherwise, exist to financial institutions developing any of these products or incentives themselves?

Lenders such as building societies are subject to a range of regulatory constraints which potentially limit their exposure to lending for environmental improvements. There are limits[1] to the amount of lending that individual lenders can provide for self-build (in construction phase) homes.

Self-build homes often contain many energy efficient features. In addition the prudential capital requirements for mortgage lending, as defined by the Capital Requirements Directive IV (CRD IV), do not make any allowance for the energy efficiency performance of the property.

Our experience, with very low levels of mortgage defaults since we were established, shows that these restrictions, when combined with appropriate specialist mortgage underwriting experience, may be too cautious and do not necessarily reflect the real risk for this type of mortgage lending, particularly where the energy efficiency improvements may have a positive impact on property valuations. We would welcome consideration of mechanisms to relax these regulatory constraints.

17. How could Government assist financial institutions with a retail presence, local authorities and other actors to run trials of these ideas?

We would be interested, in principle, to work with the Government and other partners on developing some of these ideas further and potentially supporting trials.

Price signals to encourage homeowners to prioritise energy efficiency

19. What price signals would best drive uptake of energy efficiency measures?

We believe that our range of C-Change discounts (as outlined in the introductory section) provide a positive price signal to incentivise the installation of energy efficiency improvement measures.

We would also welcome the consideration of changes to fiscal policies (such as the VAT on energy improvement measures or further reform of the stamp duty land tax (SDLT) regime) to provide a positive price signal to incentivise the installation of energy efficiency improvement measures.

Creating the conditions so that those who derive value from energy efficiency can be key players in the market

31. What are mortgage lenders' plans for improving the way they factor energy efficiency into lending decisions?

We believe our 'C-Change' mortgage discounts approach (as outlined in the introductory section) provide an effective mechanism to factor energy efficiency into our lending decisions, given the level of discount is based on the homes' energy performance. We would be happy to share details of our approach with other lenders.

In addition we also believe that innovative and modern methods of construction such as off-site construction offer new opportunities to engineer energy efficiency into the build process. We've included innovative construction materials such as SIPs (Structural Insulated Panels) in our lending criteria for many years and we recognise the BOPAS (Buildoffsite Property Assurance Scheme).

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[1] Bank of England Prudential Regulation Authority Supervisory Statement on Supervising building societies' treasury and lending activities (SS 20/15)

32. What support would lenders need in order to be able to commit to a voluntary target for improving the average energy efficiency of the properties they lend to?

In the first instance we believe there is a case for establishing greater transparency through reporting, by lenders, of the energy efficiency of mortgaged properties.

We would be happy, in principle, to work with the Government to establish the feasibility of a voluntary target for improving the average efficiency of the properties used to secure mortgages. It is important that any target includes a focus on the mechanisms for lenders to deliver positive incentives to reward energy efficiency improvements and does not result in any unintended consequences which might make it more difficult to secure a mortgage on properties with low energy efficiency performance.

In addition we recognise that the mortgage market is diverse and includes specialist lenders, such as Ecology, which focus on discrete segments of the wider market. Any voluntary target would need to take this diversity into account.

33. How can lenders develop a more accurate model of fuel bill savings, and would they be willing to lend 'green mortgages' on this basis?

While the work of the LENDERS project, as set out in the call for evidence, clearly has potential to help mortgage providers more accurately reflect the real costs of fuel bills in affordability calculations, it is important not to overstate the impact of reducing bills on mortgage affordability. In any case, our bespoke underwriting approach means that, on a case by case basis, we already consider the expected reductions in mortgage costs resulting from our 'C-Change' discounts which often significantly outweigh any fuel cost savings.

We believe our 'C-Change' mortgage discounts (as outlined in the introductory section) provide a compelling alternative approach for green mortgages given the level of discount, once any improvement works have been completed, is based on the homes' energy performance achieved and remain for the duration of the mortgage term.

34. What other changes would encourage lenders to offer more 'Green Mortgage' products?

Both the European Commission and Parliament have recently indicated they are considering mechanisms to support preferential capital treatment for 'green' mortgage lending as part of a range of interventions to support sustainable finance. It is important that that the UK Government's regulatory regime reflects any such changes to ensure that we have access to the same capital treatment of green mortgages following our exit from the EU.

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