1 Introduction

1.1 The Association for the Conservation of Energy is a lobbying, campaigning and policy research organisation, and has worked in the field of energy efficiency since 1981. Our lobbying and campaigning work represents the interests of our membership: major manufacturers and distributors of energy saving equipment in the United Kingdom. Our policy research is funded independently, and is focused on four key themes: policies and programmes to encourage increased energy efficiency; the environmental benefits of increased energy efficiency; the social impacts of energy use and of investment in energy efficiency measures, and organisational roles in the process of implementing energy efficiency policy. We welcome the opportunity to respond to this consultation paper, and would be pleased to provide further details on any of the points raised should that be helpful.

1.2 Before listing suggested policies and instruments, the Association would like to draw attention to the context in which they will operate. The consultation paper makes very clear the Government’s existing policy of minimising VAT charged on domestic fuel will continue. Government policy has also been to keep fuel costs as low as possible in the domestic sector. While there are understandable social and fuel poverty reasons for following this policy, its impact on energy saving is not to be underestimated. Clearly the more fuel costs, the more likely people are to invest in technologies and products that save fuel. Conversely the cheaper it is, the less attractive are these investments.

1.3 While it is quite clear that the Government are not seeking to consult on issues surrounding domestic fuel taxation, it is important that the impacts of the Government’s policy decision in this area are recognised. Effectively we start from a position where the taxation of fuel provides less incentive to invest in energy efficiency in the UK than any of our competitor countries in Europe. The Association believes the size of this barrier – which has been described as tying one hand behind our back before we even start – must be recognised in taking forward any instruments or policies arising from this consultation.

2 Clear overall policy objective.

2.1 The Association believes a clear overall object for the Government’s domestic energy efficiency policy is required. We commend the target suggested by the PIU of a national 20% target for energy efficiency improvement by 2010 (based on current levels).

2.2 The Association’s members, and other actors in the energy efficiency market, require a firm and unequivocal target to plan the investment and business expansion that will be required to deliver the materials necessary for the “step change” in energy efficiency activity that the PIU target requires. A firm target provides the market confidence necessary for long term investment in product, plant and personnel. Recent Government statements and actions have very much undermined this confidence1 – Ministerial denials that the longstanding HECA target (virtually identical to the PIU target) is a target have undermined confidence.

1 The Governing Council of this Association, representing major companies involved in the market for energy efficiency, issued a statement in July 2002 saying “Business plans long-term investment upon the basis of trust in Government policies and objectives. The 30% domestic energy efficiency target has been a firm Government objective for over 5 years; this has guided our investment. If the Home Energy Conservation Bill does not become law because it seeks to confirm this target, this will cause a serious erosion of business confidence in the reliability of Government. This may well have a deleterious effect on our ability to plan and invest long-term in carbon dioxide reducing measures.”
2.3 There are of course important environmental and social reasons for setting and achieving the PIU targets. Meeting these targets would assist the eradication of fuel poverty, and would cut CO2 emissions from the domestic sector – important in combating climate change.

3 Correcting market distortions caused by VAT on energy saving materials and products

3.1 Currently VAT is charged at 5% on domestic fuel, yet a number of energy saving products have a VAT rate of 17.5%. The tax system is therefore taxing energy conservation more favourably than energy consumption – a nonsense in environmental policy terms.

3.2 The Government has made some progress in equalising VAT rates, however a number of anomalies remain, and the reductions could go further.

3.3 VAT rates could be cut to 5% on:
- All energy saving materials installed under Government grant schemes
- All energy saving materials installed in non-grant schemes when householders employ contractors.
- All energy saving materials purchased for DIY installation

3.4 Furthermore, the Government should seek to cut VAT to 0% on energy saving materials. While not currently allowed under EU rules, the Treasury should report annually to Parliament on what actions have been taken at EU level to amend EU VAT law.

3.5 The current VAT reductions on energy saving materials are complex. There appears little reason for certain energy saving materials to be sold at a reduced rate in some circumstances while others are not. It is also difficult to see why some energy efficiency materials benefit from reduced rates (i.e. cavity wall insulation) while others (i.e. low emissivity glass) do not.

3.6 Such complexity has prevented the full effect of such a reduction in price being achieved – a straightforward reduction on all products in all circumstances would be easier to operate and thus have greater effect on the size of the market. Ultimately of course this would also end the market distortion of taxing energy saving materials at 17.5% while VAT on energy use is 5%.

3.7 On DIY, we would argue that the least well off in society – those who ought to be able to benefit from the VAT reduction on energy saving materials, which was introduced as a “social programme” to improve housing – are those most likely to want to buy DIY products. The Association believe it is somewhat perverse to allow a wealthy householder paying a contractor to install energy saving products to benefit from a reduced rate of VAT, but not allow a less well off household fitting the materials themselves to save money the same opportunity. The discrepancy is also a clear market distortion in terms of the DIY market versus contractors.

3.8 On the eventual aim of a VAT reduction to 0%, it is understood that this is currently outside EU law. However, Ministers have supported a zero rate and committed to persuade the EU to allow it. Our proposal for an annual report would ensure that this remained at a reasonable level of priority in Government actions, and progress was reported to Parliament to allow scrutiny of their efforts in the EU.

4 Grant subsidies on innovative products

4.1 The Government has already used grants to stimulate the market for new technologies through, for example, the current 50% grants for photovoltaic installations. Such policies do help speed
products through the initial high-cost, low volume period of their production, meaning the products can reach a self-sustaining price more quickly. With innovative energy saving materials the societal and environmental benefits of this are such that Government assistance at early stages are justified.

4.2 Current candidate technologies for support are micro-combined heat and power systems, and heat pumps. Clearly the list would be reviewed to take account of emerging technologies. A commitment to support new technologies in this way would also signal to industry that it is worth investing in research to develop even better technology in the future.

5 Enhanced capital allowances

5.1 Companies’ investing in domestic energy saving equipment should be allowed to write off their investment against tax in a single year. As a further incentive for innovative products, >100% allowances could be allowed on innovative market-leading products (again such as micro-CHP, heat pumps etc.) The measure would particularly benefit Registered Social Landlords and could stimulate the development of Energy Service Providers, who are currently finding it difficult to compete with regular energy providers because of the rules allowing householders to change supplier in 28 days.

5.2 This is virtually revenue neutral– but helps considerably with the cash flow of companies investing. We are advised by the National Housing Federation, this measure would encourage investment by RSL’s.

5.3 The scheme could of course be based upon the existing scheme allowed on heating systems under the Affordable Warmth Programme and for non-domestic energy service providers, thus removing another anomaly.

6 Stamp Duty rebates

6.1 Research studies and by the Building Research Establishment show that the time when people are most likely to invest in energy efficiency is when purchasing and moving into a new home. The Stamp Duty paid on the majority of house transactions provides an opportunity for rebates, or a fund for grants to encourage owners to put energy efficiency up their list of priorities in the initial alterations and/or renovation of their new home.

6.2 There are a number of options that could be used to operate the scheme. While a straightforward rebate is one option, the Association understands that Stamp Duty is a straightforward and easy to administer tax and there is likely to be reluctance to complicating this.

6.3 A straightforward alternative however, would be for a Government agency (such as the Energy Saving Trust) to administer a grant scheme, where proof of payment of Stamp Duty and proof of work carried out must be supplied in order to trigger payment of a grant. The grant could be set at the level of Stamp Duty paid, or some percentage of it.

6.4 The point has also been made that people buying cheaper houses do not pay Stamp Duty and so would be discriminated against. There are two points to make here. One, those receiving the grants are not actually benefiting financially from a rebate or grant – they are simply spending money on energy saving measures instead of as a tax on their transaction. The second is that a

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2 Evaluating the effectiveness of the Home Energy Report, Rosie Parnell, Sheffield University, September 2001, BRE have reached similar conclusions.
grant scheme could also pay money to people buying houses without paying Stamp Duty, though eligibility criteria would need to be different. This could still be funded through Stamp Duty by allowing those paying to reclaim only at 75% of their Stamp Duty and using the remaining 25% to subsidise new homeowners buying cheaper properties.

6.5 The grants could be made revenue neutral by increasing stamp duty – a move that would be politically acceptable as it would be made clear that people had the opportunity to avoid paying the extra tax by “doing their bit” for the environment.

7 Tax allowance against profits/surplus for landlords

7.1 These tax allowances could apply to both private landlords and Registered Social Landlords to effectively reduce the cost of energy saving materials.

7.2 The private sector has the highest incidence of fuel poverty and is the least energy efficient sector of the housing stock. Allowing landlords to claim costs of energy efficiency measures a business expense is therefore a way of both encouraging investment. This measure also compliments the Government’s stated policy of requiring landlords to improve properties in order to obtain the necessary licenses to operate (for Houses in Multiple Occupation) – providing the “carrot” to match a licensing systems “stick”. It is also something of a distortion to require investment by small businesses by means of the licensing scheme, but to refuse to allow this as a business expense.

8 Personal tax allowance

8.1 The Association does believe that this is a desirable policy, though there are of course limits to its effectiveness. We are certain that some people would claim tax rebates on energy saving materials which would increase demand, and thus save energy. As this is likely to be an option taken by the relatively well-off, rather than the fuel poor, in the households in which it is taken up it is likely to lead to significant energy savings, rather than see improvements used to increase comfort levels.

9 Council tax reduction for approved SAP increases.

9.1 By allowing councils to reduce council tax levels on homes that have had their energy efficiency improved, the financial payback of energy efficiency work could be improved, and the potential savings amplified, making people more likely to carry out energy efficiency improvements. Government policy has been to drive down fuel prices, to cut VAT on fuel and to make it clear that no tax will be charged on domestic fuel in the future, thus reducing the financial incentive for energy efficiency work (as referred to in our introduction). By enabling energy efficiency work to unlock savings in another area of household expenditure the effect of this fall in fuel prices will be mitigated. The council tax reduction could be limited to 3 or 5 years as appropriate.

9.2 Rebates have previously been used to encourage council taxpayers to help the council operate effectively - Brent Council has provided £10 rebates to encourage recycling, and a number of councils provide rebates for prompt payment.

9.3 Clearly councils will need to make up their revenue shortfall, this could be achieved by allowing increases in council tax across the board, or by providing money from central Government through adjustments to the SSA formula.
9.4 With a number of different approaches possible, support for a number of pilot schemes could be used to identify the most effective scheme.

10 **Treasury funding for local authority energy manager**

10.1 Numerous reports have made the case for dedicated local authority staff working on energy efficiency\(^1\). Since the Home Energy Conservation Act 1995 was passed, we have direct experience of the effects dedicated staff can have. HECA officers have demonstrated they can lever in spending of around 7 times the cost of employing them. This boosts local markets and local jobs in local small industry. The Energy Saving Trust found evidence that “many of the jobs were created in manual occupations in areas of high unemployment.”

11 **Tax incentives for energy efficiency companies**

11.1 Certain parts of the energy efficiency industry have already seen demand exceeding the level of trained staff – notably those fitting gas heating systems. It is important in delivering the “step change” in energy efficiency that the PIU correctly describe as necessary, that industry capacity building be supported and there are a number of ways in which this could be done. We suggest the treasury considers:-

- tax allowance for companies training installers;
- grants payable to trainees (along the lines of current grants to trainee teachers);
- tax incentives for investors in energy efficiency companies, perhaps similar to the Enterprise Investment Scheme.

11.2 Points (a) and (b) are reasonably self explanatory – they would encourage companies to train staff and potential trainees to choose this area of work.

11.3 Point (c) may require a little more explanation. Our suggestion is that the current tax breaks available for investment in innovative companies is extended to cover investment in companies promoting energy efficiency. This could be restricted to investment in new innovations in energy efficiency (e.g. Micro-CHP or heat pumps), in new approaches to energy efficiency service provision (e.g. Energy Service Companies), or to all companies providing services or products that save energy. In the final case, the scheme might be renamed the “Energy Efficient Investment Scheme”.

11.4 As an example, Unit[e] have come forward with an innovative way of marketing renewable electricity to households by promising to build new renewable generating capacity (predominantly wind and small-scale hydro-electric) to meet the demand of their customers. When their parent company decided to raise more money through a further share issue, investors were able to offset their investment in the new shares against tax, (provided certain conditions on resale periods were met).

11.5 This is to be applauded, but should be expanded to cover energy efficiency investments.

12 **Winter fuel allowance**

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\(^1\) E.g. “Monitoring the implementation of the Home Energy Conservation Act,” DETR, September 1999; Draft proposal from the 2001 review of HECA, DEFRA (unpublished as yet). The Local Government Association and by the UK HECA Forum have also called for dedicated HECA officers.
12.1 While not strictly a fiscal measure, the Government does control a powerful lever that could lead to large potential investments in energy efficiency. The Winter Fuel Payment (WFP) is available to all pensioners, regardless of needs or housing condition, each year.

12.2 While it is clearly an important payment to some pensioners in meeting their fuel bills – and the Association of course recognises the particular vulnerabilities of the elderly to cold related illnesses – there is little doubt that many pensioners do not need the payment in order to meet their fuel bills.

12.3 The Association believe that a proportion of these pensioners could be persuaded to accept a package of energy efficiency improvements in lieu of the WFP. The long term benefit to them of year on year savings in fuel bills, as well as the comfort improvements they would experience would make this an attractive package.

12.4 The exact working of such a scheme would require further development – there is a clear question whether a person becomes ineligible for WFP following receipt of such a package for just one year or for several years. There would also need to be careful planning to ensure the energy efficiency package could be delivered in a timescale that enabled the elderly households to keep warm in winter.

12.5 However, it would seem almost negligent during such a review not to examine carefully how such a significant Government spending lever could be altered to improve energy efficiency, and we encourage the Treasury to study this further.

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