

Reforming the Green Deal

October 2014

Summary

British Gas has provided ongoing and active support to the Green Deal programme since its inception. We have arranged over 300 finance plans, trained over 300 assessors, completed 100,000 assessments and carried out 13,000 installations. Our experience has highlighted several challenges with the Green Deal proposition, including an over-reliance on Green Deal finance to drive demand, and a complex customer journey.

We support the Government's objective to create a significant, paid-for market for energy efficiency improvements. However, the success of this market depends on the creation of significant customer demand. This demand has not been stimulated to date, and has been hindered by a focus on the finance mechanism. We therefore believe there should be a **renewed focus on driving customer demand**.

To create this demand, energy efficiency policy needs to take customers as its starting point and be built on a deep understanding of their needs and behaviours. Our experience suggests that long-term demand for energy efficiency needs to be driven by incentives, regulation, or both. Without this, customers will simply not make their homes more energy efficient.

The role of Green Deal finance

Green Deal finance was intended to overcome perceived financial barriers to the uptake of energy efficiency measures. It reflected the belief that untapped customer demand existed for energy efficiency improvements, but was held back by the lack of a suitable finance product. Despite the introduction of Green Deal finance, this assumed customer demand has not materialised. Take-up of Green Deal finance has been further hampered by the complexity of the process, and the restrictive 'Golden Rule'.

We understand the attractions of the pay-as-you-save (PAYS) principle; however we do not believe it will play more than a niche role, even with significant reform. The key benefit of PAYS is that it can provide finance to those who would otherwise struggle to borrow. However, customers who need PAYS are constrained by the Golden Rule, which limits loans to around 30% of installation costs. While this funding gap could be bridged with subsidy, it is significant – typically accounting for 70% of the cost of measures. We believe that any subsidy should be applied to the measures installed, and not be dependent on householders taking on what they perceive to be debt, whether it is through Green Deal finance or elsewhere.

Customers who can afford to break the Golden Rule do not need PAYS because they have the option to borrow more cheaply from other lenders elsewhere. The interest rates and charges applied by the Green Deal Finance Company (GDFC) are not attractive to those who are able to secure conventional finance at lower rates. There are many other lenders who would be keen to provide finance of this sort, should significant paid-for demand develop. For example, Nationwide already offers 'Green Additional Borrowing' to mortgage customers, with an initial interest rate of 1.89% - far below the 8-12% APR typically offered by the GDFC. The small numbers of Green Deal finance plans that have

been delivered to date have been driven by incentives such as cashback, and there is **little evidence that Green Deal finance on its own causes customers to take action.**

The GDFC has recently accepted that its current business model is not sustainable, and while we agree with this assessment, we are considering the merits of their new business plan. It does little to address demand creation, yet assumes a paid-for market ten times larger than that being created by the Green Deal Home Improvement Fund (GDHIF). Finance is an enabler of demand, and will not create demand where previously there was none.

Driving demand

The Green Deal **demand that we have seen has been driven by incentives.** Customers are attracted by the 'Deal' in Green Deal, and will act if it is sufficiently compelling. For most, a 'deal' means cashback or money off. It doesn't mean a loan, however innovative. British Gas has delivered more than 13,000 measures through the Green Deal, and all of these have been driven by incentives. The offerings of other market participants rely heavily on incentives, in both marketing and customer proposition.

While the early closure of the GDHIF was disappointing, we welcome the overall approach and the intention of creating a compelling customer offer. While we welcome the recent announcement of further funding for the scheme, the GDHIF is finite, and it relies on significant taxpayer funding. The creation of sustainable, **long-term demand for energy efficiency measures can best be driven by a combination of both 'carrots' and 'sticks'**. This could include taxpayer-funded offers, fiscally neutral incentives such as variable stamp duty and council tax, or regulation; for example, by building on current legislation targeting the private rented sector.

Reforming the Green Deal framework – including simplifying the customer journey, Green Deal finance and PAYS – will not lead to significant demand for paid-for energy efficiency measures. Government should focus on the role that could be played by incentives and regulation.

Green Deal assessments

While the majority of the 320,000 Green Deal assessments delivered in total to date have been followed by the installation of an energy efficiency measure, **there is little evidence that the assessments themselves create demand.** Assessments are typically driven by the need to secure funding for installations that are already planned; this has been the case for the Energy Company Obligation, Green Deal incentive schemes and the Renewable Heat Incentive.

Of the 100,000 assessments we have carried out, only 6,000 have been for customers not already engaged in buying a measure, and few of those have resulted in an installation. While tailored energy efficiency advice can play a role in building demand, Green Deal assessments lack product information, a clear 'call to action' or advice on behaviour change. They are lengthy, expensive, and can be intrusive. Advice should be personalised, interactive, action-oriented and free.

We believe that **an engaging online service could meet the needs of most customers** - which would be cheaper, simpler and quicker - and that consideration should be given to how this might be developed as a substitute for the current Green Deal assessment.