

**Business, Energy and Industrial Strategy Committee Energy Efficiency Inquiry**

**Written Submission from ARLA Propertymark**

**January 2019**

**Background**

1. ARLA Propertymark is the UK's foremost professional and regulatory body for letting agents; representing over 9,000 members. ARLA Propertymark agents are professionals working at all levels of letting agency, from business owners to office employees.
2. Our members operate to professional standards far higher than the law demands, hold Client Money Protection and we campaign for greater regulation in this growing and increasingly important sector of the property market. By using an ARLA Propertymark agent, consumers have the peace of mind that they are protected, and their money is safe.

**Existing housing stock**

Are the Government's targets to improve the Energy Performance Certificate (EPC) ratings of our existing housing stock ambitious enough?

3. ARLA Propertymark believes that the Government's targets to improve the EPC ratings of our existing housing stock are too ambitious. This is because, in order to raise all private rented properties EPC to C by 2030, this will require either a major refurbishment or significant works to be carried out on privately rented homes which comes at a substantial cost to the landlord. We would argue that instead of focussing on the EPC targets set out in the Clean Growth Strategy, the Government should instead move towards a property MoT,<sup>1</sup> that encompasses many elements of property standards including energy efficiency.
4. Private landlords have little access to funding outside of their own income in order to make energy efficiency improvements to their properties. Ambition and setting targets for improving energy efficiency are meaningless if opportunities and support are not offered in order to achieve them. To reach the Government's targets to improve the EPC ratings of our existing housing stock, better funding and support will need to be provided to landlords with

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<sup>1</sup> <http://www.nationwidefoundation.org.uk/wp-content/uploads/2018/09/Private-Rented-Sector-report.pdf>

an incentive to make the changes, otherwise it is likely that landlords will sell properties that are not financially viable to improve.

5. Rather than aiming for the EPC targets indicated in the Clean Growth Strategy for existing privately rented housing stock, the Government should instead introduce a mandatory property 'MoT'. Similarly to a motor vehicle MoT, the property MoT would require a home to meet a minimum set of requirements before it can be rented. The annual MoT would "integrate the existing range of requirements with regard to electrical and gas safety and energy efficiency, but also include assessment according to a basic minimum standard for habitation check."<sup>2</sup> Not only would the MoT reinforce the property's energy efficiency requirements, but it would also tackle further issues in substandard privately rented properties. This is beneficial in three ways. Firstly, for tenants, as they can be confident in the standard of their home. Secondly, landlords will have greater clarity on their responsibilities and be able to deduct the cost of the MoT from Income Tax. Finally, rogue landlords will be deterred away from the sector enhancing the quality of properties within the private rented sector.

Is there sufficient support in place to deliver targets for all homes to be EPC band C by 2035?

6. No, we do not think that there is sufficient support in place to deliver targets for all homes to be EPC band C by 2035. This target will be reached in the social rented sector, as there is more than enough support provided for that tenure. However, there is an inadequate amount of support provided for private homes in general and particularly the private rented sector; meaning there is little incentive for landlords to make energy efficiency improvements to their properties. Therefore, without further provision of support for the private sector the Government's targets will not be achieved.
7. It is likely that this target will be reached within the social rented sector. Existing Government backed funding initiatives largely focus on existing social rented stock, despite it being the smallest tenure accounting for only 17% of housing stock in England according to the English Housing Survey 2017/18<sup>3</sup> and having the highest number of homes with the most energy efficient EPC ratings of A, B and C. Billions of pounds have been given in grant aid to social

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<sup>2</sup> [Ibid.](#)

<sup>3</sup> [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/724322/Social\\_rented\\_sector\\_report.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/724322/Social_rented_sector_report.pdf)

landlords whereas private landlords have barely benefitted from any funding. This is despite the increasing number of low-income households living in privately rented property due to the lack of available social housing. Energy Company Obligation (ECO) funding is more difficult and costlier to implement when applied to the private rented sector, meaning that landlords can find it difficult to access. For example, one social housing provider with 1,000 units, compared to 1,000 private rented sector landlords with one unit, is a more cost-effective way for ECO companies to deliver their obligation.<sup>4</sup> We would argue that in order for the Government to achieve its objectives, ECO funding to social housing should now be stopped, and all future funding from energy suppliers should be dedicated to supporting the private sector.

8. In addition, as support provided to the private sector is completely insufficient, the target will also not be met due to the costs associated with improving the energy efficiency of a property. In a recent survey, a number of ARLA Propertymark members indicated that they advise landlords with properties that have E, F and G EPC ratings to sell the property as the cost implications of improving the property (unless it is exempt or listed) are often too high to warrant and little to no financial support is made available to them. The Government claims that the average cost to landlords to make energy efficiency improvements to reach EPC E alone will be £1,200.<sup>5</sup> However, recent research conducted by the Residential Landlords Association suggests that landlords of properties with an EPC rating below E believe that it would cost them on average £5,789.72 to bring their property up to the regulatory standard, which is currently EPC E.<sup>6</sup> The same research indicated that 23% of landlords are planning to sell their properties within 12 months, and that a third of them cannot afford to bring their properties EPC up to an E rating.<sup>7</sup> Associated costs with making energy efficiency improvements are encouraging landlords to decrease their portfolios or exit the sector altogether. It must also be noted that should landlords sell their most energy inefficient properties and these homes move into the owner-occupied sector, whilst the private rented sector's energy efficiency might improve, it will result in the owner-occupied sector's energy efficiency declining meaning that the Government's target for all homes to reach EPC C by 2035 will still not be achieved.

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<sup>4</sup> <http://www.arla.co.uk/media/1046836/consultation-to-amend-the-energy-efficiency-regulations-2015.pdf>

<sup>5</sup> <http://www.arla.co.uk/news/november-2018/landlords-foot-the-bill-to-bring-properties-up-to-energy-efficiency-standards.aspx>

<sup>6</sup> <https://research.rla.org.uk/report/examining-energy-efficiency-electrical-safety-in-the-private-rented-sector/>

<sup>7</sup> [Ibid.](#)

9. Further, additional tax changes for landlords' act as a further deterrent to make energy efficiency improvements to their properties. Up until 6 April 2017, landlords could deduct mortgage interest and any other costs associated with renting a property before determining taxable profit. From 6 April 2020, Mortgage Interest Relief will no longer apply, and the only Income Tax relief that landlords will be able to get on residential property finance costs will be capped at the basic rate of tax (currently at 20%).<sup>8</sup> Under the changes brought in by Section 24 of the Finance Act 2015, thousands of landlords will pay more tax. The change will push many landlords up a tax band despite their income not increasing as tax will be applied to turnover instead of profit. To cover the additional taxes landlords will increase rents for new and existing tenancies. They will also cut back on other expenses such as energy efficiency improvements and property maintenance. Further, landlords are required to pay a 3% surcharge on Stamp Duty when they buy a property and can no longer claim 'Wear and Tear Allowance' on their properties; both increasing costs which results in less money being available for improvements such as energy efficiency. All the extra tax mounts up and is encouraging landlords to sell up altogether and leave the sector.<sup>9</sup> Research by the National Landlords Association indicates that around 19% of landlords intend on selling their buy to let properties.<sup>10</sup> Landlords exiting the sector produces a shortfall in much needed private rented homes and makes the cost of renting more unaffordable for fuel poor homes.

Is the Energy Company Obligation (ECO) an adequate mechanism to ensure fuel-poor homes are upgraded to EPC band C by 2030?

10. No, we do not believe that the Energy Company Obligation (ECO) is an adequate mechanism to ensure all fuel-poor homes are upgraded to EPC band C by 2030. Whilst ECO goes some way in achieving energy efficiency requirements in socially rented homes, it does little to improve owner occupied and or private rented stock for two reasons. Firstly, it works on the basis of the inhabitant's income rather the building's EPC rating. Secondly, in the private rented sector, it is not the responsibility of the tenant to maintain or improve the fabric of the building. Taking this into consideration, ECO has to date and will continue doing little to improve the energy efficiency of fuel-poor homes that are not socially rented.

<sup>8</sup> <http://www.arla.co.uk/media/1046918/restriction-of-financial-costs.pdf>

<sup>9</sup> <http://www.arla.co.uk/media/1047267/overcoming-barriers-to-longer-term-tenancies.pdf>

<sup>10</sup> <https://landlords.org.uk/news-campaigns/news/good-news-first-time-buyers-bad-news-renters>

11. ECO in its previous incarnations and existing format (ECO3) has been an adequate mechanism for upgrading the EPC of fuel-poor socially rented homes. The current iteration requires that social housing only needs to have an EPC rating of F, G or E to access funding from the ECO under the Home Heating Cost Reduction Obligation (HHCRO), or Affordable Warmth Obligation.<sup>11</sup> Upon permission from the social landlord, works will then be carried out on the property. The criteria for eligibility do not require for the social tenant to have a certain income and only relies on the energy efficiency of the property. Thus, this makes the funding very easily accessible for social tenants in homes that are the least energy efficient.
  
12. ECO is not an adequate mechanism for upgrading the EPC of fuel-poor privately owned homes because rather than focusing on the energy efficiency of the property, it focuses on household income. Although it is the intention of the latest iteration of the scheme to focus on household income,<sup>12</sup> it contradicts the goal of upgrading fuel-poor homes to EPC band C by 2030. The cost of adequately heating a home does not change depending on the income of the occupant; a tenant who had not previously been classed as fuel poor could easily become fuel poor by moving to a less energy efficient property despite their income not changing at all. To this end, the Government should prioritise energy efficiency of the two largest tenures, which are also the least energy efficient, through a new Affordable Warmth Scheme.
  
13. Further, it is not the responsibility of tenants in the private rented sector to maintain or improve the fabric of their rented home. The consequence of this is that where a private tenant qualifies for ECO funding, they must have the landlord's permission for the work to be carried out.<sup>13</sup> Part Two of the Energy Efficiency (Private Rented Property) (England and Wales) Regulations 2015 allows private tenants to request permission from their landlord to make improvements where the tenant is able to secure funding. In order for private landlords to access Affordable Warmth funding, the tenant will need to be in the property from the day of assessment until the day of installation. If the tenant moves out, the property will no longer be eligible, and the improvement works will not be carried out, this issue is not replicated in the social rented tenure as ECO funding works on the basis of the energy efficiency of the home rather than the income of the tenant. ECO will go little in the way to improving the

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<sup>11</sup> <https://www.ofgem.gov.uk/publications-and-updates/eco3-social-housing-e-f-and-g-declaration-and-landlord-permission>

<sup>12</sup> <https://www.ofgem.gov.uk/environmental-programmes/eco/about-eco-scheme>

<sup>13</sup> <https://researchbriefings.parliament.uk/ResearchBriefing/Summary/SN06814>

energy efficiency of private homes unless it makes the property's EPC the main criteria to access funding rather than the income of a potentially transient occupier. To incentivise landlords with the least energy efficient properties to make improvements and consequently reach targets, funding from ECO for social housing should stop and eligibility for private housing for ECO should be based on EPC ratings.

### **Private rented sector**

#### Are the Government's private rented sector regulations for energy efficiency for both residential and commercial buildings ambitious enough?

14. ARLA Propertymark believes that the Government's private rented sector regulations for energy efficiency for residential buildings are too ambitious, and will not be achieved, due to the cost implications being too high. With the collapse of the Green Deal, the only Government scheme ever designed to overcome the "Split Incentive" (the landlord pays for the energy efficiency improvements and the tenant benefits from a reduced bill) the Government must act to ensure landlords can comply with the proposed energy efficiency targets. The Government needs to reconsider its decision to introduce a landlord contribution element where funding is unavailable to ensure that improvement to properties (currently where they are rated F or G) can be delivered. In order for the Government's targets to be more realistic, it must provide better funding options for the private rented sector and cease the funding currently provided to social housing. Without incentives or accessible funding, it is likely that targets for the private rented sector will not be met and rather than improving the properties, landlords will opt to sell off their low energy efficiency stock; transferring the problem to a different housing tenure rather than solving the problem and achieving the Government's aim.

15. We believe that without better funding options available for private landlords, the regulations are too ambitious. It is unrealistic to assume that landlords will feel willing to keep continually making energy efficiency improvements to their properties every time the EPC rating requirement rises due to the associated cost to landlords and a lack of available funding. As aforementioned, the private rented sector is the second largest tenure with the highest number of the least energy efficient homes, yet it receives the least amount of funding.

Funding needs to be directed towards the private rented sector if the Government wants to achieve the energy efficiency targets set out in the Clean Growth Strategy.

Are there implementation and enforcement challenges that need to be remedied?

16. Yes, we believe there are implementation challenges that need to be remedied in order to make progress in private rented sector energy efficiency. Firstly, the Government is moving away from the principle under the Energy Act 2011 that there should be “no upfront costs” to private landlords. Secondly, the announced landlord’s contribution to make energy efficiency improvements of up to £3,500 is too high.<sup>14</sup> Thus, to remedy these discrepancies, the Government should do two things. Support should be provided to private landlords by reintroducing the Landlord’s Energy Saving Allowance (LESA). Further, the Government should extend the LESA to include anything contained within the Recommendations Report of an Energy Performance Certificate (EPC). By reintroducing LESA, landlords will then be able to offset the costs of energy efficiency improvements against income tax for the financial year in which the costs were incurred rather than having to wait until the property is sold before being able to offset the energy efficiency costs against Capital Gains Tax. This will significantly assist landlords with the costs of the improvements and their financial planning.
17. We do not agree with the Government’s decision to require landlords to contribute up to £3,500 per property to make energy efficiency improvements to ensure that the home is a minimum of EPC E. Under the Energy Act 2011, the Government pledged to avoid ‘upfront costs’ for landlords; which has now been disregarded by setting a cost cap as high as £3,500. In many parts of the country, £3,500 equates to around seven months rent. Leveraged landlords (those with a mortgage) will find it very difficult to find this sum of money when average net profits for the sector are around 2-3%. Therefore, the cost cap at this level will act as a direct disincentive for landlords to make energy efficiency improvements to their property and again, will sell them into the owner-occupied sector and then purchase more energy efficient properties if they wish to continue as a landlord. This does not solve the Government’s problem; it merely pushes it somewhere else.

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<sup>14</sup> <http://www.arla.co.uk/news/november-2018/landlords-foot-the-bill-to-bring-properties-up-to-energy-efficiency-standards/>