“REFORMING THE BUSINESS ENERGY EFFICIENCY TAX LANDSCAPE” CONSULTATION RESPONSE

ABOUT THE UK-GBC AND OUR RESPONSE TO THE CONSULTATION

The UK Green Building Council (UK-GBC) is an independent, membership-based, not-for-profit organisation committed to dramatically improving the sustainability of the built environment by radically transforming the way it is planned, designed, constructed, maintained and operated. This consultation response was developed following a number of workshops held with members both in the lead up to and during the consultation.

As an overarching comment, we would like to emphasise that this review represents an unprecedented opportunity for the Government to create an effective and coherent energy efficiency policy landscape. If successful, the resulting activity could have enormous benefits for the UK in terms of increased productivity, enhanced energy security, and reduced greenhouse gas emissions. This opportunity is all the more important in the context of recent cuts to, or failures of, related policies covering new buildings, renewable generation, and home retrofit.

However, in order to achieve this, it is vital that the clear focus is on effectiveness, rather than the process being dominated by a short-term desire to cut business burden. By failing to drive improvements in UK businesses’ energy efficiency, we will be exposing our economy to greater harm in the future, and putting the long-term health of our economy at risk. Conversely, a resource efficient business sector will help to create a vibrant, low-carbon UK economy that is fit for the future.

UK-GBC ANSWERS TO THE CONSULTATION QUESTIONS

1. Do you agree with the principle of moving away from the current system of overlapping policies towards a system where a single business/organisation faces one tax and one reporting scheme? Please provide evidence on level and types of benefits of an approach like this.
In recent years there have been regular calls from industry and other stakeholders – ourselves included – to simplify the complex* climate and energy policy landscape affecting businesses, and more specifically the non-domestic buildings sector. As it stands, the number of different and varied policies affecting commercial buildings is likely to be having a negative impact on the ability of their owners, occupiers and managers to deliver energy efficiency improvements. In the presence of such complexity, a disproportionate amount of some businesses’ time can be spent on compliance, rather than being focussed on the implementation of energy-saving projects. For this reason, there *may* well be benefits in moving away from the overlaps in the current system, towards a simpler landscape. However, this general principle is subject to some important conditions. Firstly, the potential bureaucracy-reducing benefit of creating a “*one tax and one reporting scheme*” approach depends very much on what the final *one* scheme each organisation faces looks like. If care is not taken, a single scheme could be created that contains almost as much complexity as the original set, with the transition

costs (of participants learning how to comply with a new scheme) more than offsetting the benefits of simplification. Deregulation and better regulation are far from being the same thing.

Secondly, and linked to the preceding point, it is vital to consider the *net benefit* of the simplification process rather than focussing solely on the bureaucratic burden. Removing complexity/burden *could* also come at the expense of removing scheme features that drive genuine change. The current schemes all have their own merits, and it is by no means guaranteed that a single, simple scheme would necessarily incorporate all or most of its predecessors' most powerful levers for action for a given organisation. As such, a single scheme may well be *simpler*, but may also be less effective in driving investment in energy efficiency if care isn't taken in its design. The vast majority of the organisations set to be covered by the most substantive elements of a reformed landscape are large and sophisticated enough to be able to deal with a reasonable degree of policy complexity, and to make use of lessons learned from participation in current schemes to achieve compliance in the future.

Thirdly, it is worth noting the simplification is not necessarily just about reducing the *number* of policies faced by organisations - it can also be achieved by focussing on the data used for compliance. As concluded in the Green Construction Board's recent and insightful "*Bigger, Better Data*" report**, a significant reduction in the overall policy framework's bureaucratic burden in this space could be achieved simply by taking steps to ensure that participants were better able to use the same dataset – albeit perhaps cut in different ways – to achieve compliance with a multitude of different individual policies (particularly in respect of reporting). This is not something that the current framework, with its varying scopes and timeframes, is well designed to support, and it would be welcome if this review could help to drive not only greater levels of energy measurement and reporting, but also greater consistency across policy and practice. This would not only have benefits for the participants, but would also help to foster a better understanding of buildings and how they operate, and underpin more informed and better-targeted policy-making.

Finally, it is important for policy-makers to be aware of the hindrance to investment that is created by regular *changes* to policy. Over recent years, the constant changes that have affected the business energy efficiency policy landscape are likely to have been just as damaging to progress as the degree of overlap between the various elements. Each time changes are made, additional burden and cost is placed on participants. As such, it is vital that these reforms are undertaken with the long-term in mind. There is little benefit from, for example, creating a new landscape the ambition of which is not commensurate with our climate and energy needs, and which therefore needs to be changed soon after it is put in place.

However the simplification is ultimately achieved there are some key principles that the final outcome must satisfy:

- **Ambition** – as stated in the consultation document, the final landscape must improve the business case for investment in energy efficiency if we are to deliver a more productive, efficient, low carbon economy. It is extremely unlikely that simplification alone will achieve that aim.
- **Consistency** – as stated above, creating a new regime that has longevity is absolutely critical. It should be consistent with the UK's long-term climate and energy goals, to avoid the risk of near-term changes disrupting investment.

- **Transparency** – the final policy mix should make it easier for participants and external stakeholders to understand how their energy performance compares to their peers and to invest accordingly
- **Visibility** – the drivers for action under the new landscape must be clear and visible, so that they attract the attention of senior decision makers
- **Complementarity** – while this review is relatively broad in its scope, it does not directly cover important, complementary policies. As such, it is important that the final design of the improved energy efficiency tax/reporting/incentive schemes not only interact effectively with one another, but also with the wider policy landscape.

In relation to the latter, it is particularly important that Government considers how these policies interact with the potentially hugely influential Minimum Energy Efficiency Standards (MEES) for non-domestic buildings, and the related Energy Performance Certificate regime. Properly implemented and enforced, these policies could play a critical role in supporting better outcomes from the reformed Energy Efficiency Tax (/reporting) landscape.

*For more detail on the wide range of policies affecting non-domestic buildings, and their relative merits, see the Green Property Alliance's "*Carbon Incentives and Penalties*" report. http://www.bpf.org.uk/sites/default/files/resources/GPA-Carbon-Penalties-Incentives-MAIN-REPORT-with-foreword.pdf

** The Bigger, Better Data report is of significant relevance to the wider context of this review, and should be considered by the policy-makers. It suggests, for example, that a code of practice governing the measurement of operational energy data in relation to buildings should be developed, supported by Government, as a key step in driving greater energy efficiency across the property sector. A copy of the report can be accessed either directly from the GCB, or from us (the UK-GBC).

2. Do you agree that mandatory reporting should remain as an important element of the landscape in driving the uptake of low carbon and energy efficiency measures? If not, why not?

It is a clichéd but nonetheless true adage that you cannot manage what you don't measure. As such, there is little doubt that schemes which mandate organisations to quantify and report their energy form an essential foundation for the uptake of low carbon and energy efficiency measures. At the top end of the property sector, the benefits of reporting can be seen in the success of schemes such as the Global Real Estate Sustainability Benchmark (GRESB) and the Better Building Partnership's Real Estate Environmental Benchmark (REEB), and the focus they have placed on measurement and management of energy and carbon performance. In the absence of a mandatory reporting framework, inertia and lack of awareness, amongst other things, can prevent these kinds of practices being implemented. This is particularly true amongst business that are smaller or otherwise less exposed to reputational drivers.

In the context of this review, it is unlikely that any of the elements of the planned regime (reporting, tax and incentive) would be sufficient to drive significant change on their own, particularly given the relatively small proportion of overall business costs represented by energy. As such, it is important that the final landscape makes use of a variety of complementary levers, rather than placing undue emphasis on the individual elements. For example, a tax that represents an additional percentage cost on top of the energy price (the CCL) could quite feasibly be quickly absorbed as an ongoing business-as-usual cost, with little visibility to senior executives. However, if this tax bill is clearly identified as part of an annual report that requires board level sign-off, which also sets out a range of energy- (and tax-) saving measures that could attract additional finance via an incentive scheme, it is reasonable to assume that it could have significantly greater impact.

While we would welcome a strengthened, ESOS-based annual reporting regime (to sit alongside the four-yearly cycle of full ESOS audits - see answers below), it is important to point out that many of our larger members have specifically highlighted the benefits that reporting under the Mandatory Greenhouse Gas Reporting (MGHGR) framework have generated across their organisations in terms of raising board-level awareness and driving action on energy efficiency and carbon emissions. There appears to be a strong case for continuing reporting of this nature for listed companies, either as a separate scheme covering these organisations, or as a size(/listing)-dependent element of a reformed ESOS. This argument is strengthened by the requirements of the EU Directive on Non-financial Reporting, which will make the measurement and reporting of these kinds of environmental data mandatory anyway for some large companies.

One key point to emphasise here is that *annual* reporting is of particular importance in the property industry. The prospect of a regular requirement to measure and report data encourages organisations to put in place effective monitoring systems, to improve metering and so on. The incentive for this may be significantly reduced if the reporting requirement is less regular. From a property perspective, portfolios change sufficiently regularly that anything less than annual reporting would be of significantly less value in terms of tracking performance. The latter, of course, is all the more vital if these reforms result in a performance-based incentive scheme.

For medium or small businesses, in-depth, annual reporting may be less cost-effective. For them, it may be worth considering a lighter touch scheme, or one that is voluntary but linked to eligibility for any incentive scheme. This could make use of the existing Display Energy Certificate (DEC) tool, which requires organisations to measure properties' operational energy use, and provides for public disclosure of the findings via their display. For more on the potential role of operational ratings under this review, see the answers to Questions 5 and 14 below.

3. Should such reports require board level sign-off and should reported data be made publically available? Please give your reasons.

There is little question that reports should be subject to board-level sign-off. Without this feature, there would be serious questions as to whether reports would gain due attention from senior executives. Board level sign-off has been an important component of the CRC, and is regularly highlighted as one of the few remaining levers within that scheme that is creating impact. It may even be worth strengthening this requirement in the new landscape, by ensuring that board-level signatories cannot devolve this responsibility to an agent/representative within their organisation, and by requiring the submission/sign-off of the report to the board to be a minuted item in company records.

Making these reports, or a subset of the data within them, publically available could also be a powerful lever for action. The CRC's league table, although unpopular with some, is widely recognised as having been a significant motivator amongst participants. While it may be unnecessary for Government to take on the role of producing league tables, making key data available from organisations' reports would allow third parties to compare (rank/benchmark) participants' performance, creating reputational pressure to act. Moreover, access to key data would enable investors understand whether companies are managing their fiduciary and operational risks, and to invest accordingly. This would help to create a transparent and efficient market, particularly if a move towards reporting at the asset (building) level could be encouraged (either through the reporting scheme, or under the incentive – see below for more detail). In deciding what data is made publically available, appropriate consideration should of course be given to that which might be genuinely commercially sensitive.

As proposed above, for those organisations currently caught by the MGHGR scheme, *disclosure* could initially remain as per the current requirements of that scheme (perhaps with the addition of energy use totals). For all other large (ESOS) organisations, we would suggest that, at a minimum, they should publically disclose their total energy use (in KWh). Additional information that could usefully be reported and made public by participant organisations might include a self-selected normalisation factor; their total (estimated*) CCL bill; and (every four years) the estimated total cost effective energy saving potential as identified in their ESOS audit. One way to encourage greater levels of disclosure may be to make some elements mandatory, while linking other voluntary components – such as the energy saving potential - to organisations' ability to access to the incentive scheme (see the answer to Question 14 below).

*Due to the potential complexities in aggregating CCL payment data (particularly if energy companies are not required to produce an annual statement), one approach could be to allow organisations to estimate their annual bill by applying to the appropriate rate to their reported gas and electricity totals.

4. Do you agree that government should develop a single reporting scheme requiring all ESOS participants (and potentially the public sector (see paragraphs 4.21 – 4.23)) to report regularly at board level? If so, what data should be included in such a report?

We broadly agree that there should be a single reporting scheme faced by each participant organisation, but there may be merit in including some diversity of approach within the single scheme to account for organisations' different size, sophistication and impact.

As set out above, for listed companies currently caught by the MGHGR scheme, we propose that they should continue to gather and report the same data on an annual basis (i.e. total GHG emissions, split by scope), whether or this is done under a continuation of the current MGHGR scheme, or as part of a new ESOS-based scheme. For those organisations that are currently caught by ESOS but not by MGHGR, their reporting requirements should be extended such that they are required to measure and report their ESOS-related energy use – as a minimum – on an annual basis.

We do not believe this would represent a significant additional burden on these organisations, since the same systems and processes put in place to undertake a full ESOS audit on a four-yearly basis *should* make it relatively straightforward to gather and report the same aggregated energy use data on an annual basis (without the need to identify energy saving measures on an annual basis). In fact, it may well be *easier* for organisations to cost-effectively keep a handle on their energy use if they report annually than if they operate under a stop-start four year cycle. Annual reporting would, as stated elsewhere, also make it much easier for them and the scheme administrators/ Government to track progress in relation to any incentive scheme, as well as providing data that could be used to develop well-targeted policy in the future.

Under our preferred approach, every four years *all* organisations would continue to be required to undertake a full ESOS *audit* to identify cost-effective energy-saving measures. We would emphasise that this would not constitute MGHGR-covered companies being faced with two *reporting* schemes, since ESOS is primarily an auditing rather than a reporting scheme.

5. The government recognises the importance of ensuring market actors have access to transparent, reliable and comparable information to support financing and investment in energy efficiency and low carbon measures. How best can a streamlined report achieve this? To what extent does your response apply to other large companies (as defined in the Companies Act) that are not listed companies?
As set out above, we strongly believe that key elements or reported data should be made publically available in order to help create a more transparent market, to leverage investor influence, and to enhance the role of reputational drivers. These benefits are not limited to listed companies only, and as such – as covered in our response to Question 3 – we believe that some key data should be disclosed by all large companies. For buildings, the holy grail of investor transparency – and something to aim for over time – is for operational performance to be publically disclosed at the asset level. Currently this is (at least theoretically) the case for larger public buildings via the DEC regime, but is not so for their commercial peers. As such, we would welcome anything that could be achieved under these reforms to encourage greater penetration of operational ratings into the market. High levels of operational rating of buildings have been shown in other countries – most notably in Australia under their NABERS scheme – to help create a vibrant market for efficient buildings, and to incentivise improvements to the stock. While it may be difficult to directly incorporate asset level operational ratings with an organisation level reporting scheme, there are other ways in which the policy landscape could support a greater focus on operational energy rating of buildings (see our answer to Question 14 for more detail).
6. Do you agree that moving to a single tax would simplify the tax system for business? Should we abolish the CRC and move towards a new tax based on the CCL? Please give reasons.
It is likely that a single new tax based on the CCL would be *simpler*, but it is not clear that it would *necessarily* be more effective. It is important to consider that the CCL is paid by a much greater number of organisations than the CRC, and thus a shift from the latter to the former – if the rate was equal across all participants regardless of size – *could* see the financial incentive effect of the tax reduced compared to the status quo. This suggests that the effective tax rates *may* need to vary across organisations (see also our answer to Question 8 for more detail) in order to retain and extend the financial impact on companies currently covered by the CRC. Furthermore, when considering the buildings sector, it is also important to remember that energy typically represents a relatively small proportion of total operating costs, and thus adding a small percentage on top of this would, on its own, offer a relatively weak price signal to building owners, occupiers and managers. This reinforces the earlier suggestion that the tax will need to work in tandem with the reporting and incentive regimes if it is to drive significant improvements.
7. How should a single tax be designed to improve its effectiveness in incentivising energy efficiency and carbon reduction?
When considering the design of the tax, Government may want to consider the principles set out in the CBI report "*The Colour of Growth*" (see page 23 here: http://www.cbi.org.uk/media/1552876/energy_climatechangerpt_web.pdf). For example, it will be critical to ensure under this reform process that the reformed CCL is

aligned with the reporting and incentive elements of the landscape ("*Strategic Fit*"); and for a trajectory to be set out to show how it will rise over time ("*Certainty to Business*"). The latter has frequently been raised by members and other stakeholders as a means through which the incentive effect of the tax could be strengthened, with the Landfill Tax escalator having been regularly cited by our members as an effective example of long-term policy-making that has driven investment. It is expected that a similar energy tax (CCL) escalator could play a significant role in enhancing the tax's effectiveness. If an escalator is introduced, steps in the rate paid should be set with reference to the recommendations of the Committee on Climate Change and the targets under the Climate Change Act, and their duration should be consistent with a reasonable investment horizon (perhaps five years). In order to help ensure that businesses have visibility over the tax they are paying, it may also be useful if energy companies were required to provide an annual CCL statement to customers. These figures could then more easily be aggregated and included in companies' returns under the reporting scheme (see our answer to Question 3 above).
8. Should all participants pay the same rates (before any incentives/reliefs are applied) or should the rates vary across different businesses? For example, do you think that smaller consumers and at risk Energy Intensive Industries (EIIs) should pay lower rates?
UK-GBC recognises that there may need to be allowances made to protect smaller businesses and those at risk of carbon leakage (which should therefore be considered in the context of wider, international progress on climate change). However, steps taken in this direction should not leave these organisations without clear incentives to invest in energy efficiency. Many SMEs, for example, are likely to have considerable "low hanging fruit" energy saving opportunities. It is unclear whether, overall, it would be more simple, effective and efficient to achieve this differentiation through the application of differential rates, or through a system of incentives/reliefs. We would welcome further analysis by HMT/HMRC to clarify which approach would be more effective. It is worth noting, however, that many SMEs do already pay CRC costs that are passed through by their landlords. Not all landlords are captured by the CRC and those that are cannot always pass through the costs, resulting in this impacting unevenly on SMEs. As such, a move towards all organisations paying the same rate could help to create a more even playing field. The impact of the tax on SMEs, and the rate they should pay, should also be considered alongside the support that may be available to them to reduce their energy usage. For example, it would be helpful for the review – as set out above – to include measures which encourage SMEs to quantify and understand their energy consumption and the related tax burden they face, so that they are better able to identify and deliver efficiency improvements (and tax savings).
9. Do we currently have the right balance between gas and electricity tax rates? What are the implications of rebalancing the tax rate ratio between electricity and gas? What is the right ratio between gas and electricity rates?
It would certainly make sense from a climate change mitigation perspective to switch to a system in which the rates paid reflected their carbon intensity. If this option was pursued, then it would be helpful if rates were announced and then retained for a reasonable period of time (perhaps five years) in order to improve investment certainty.

One unintended consequence of taking this approach, however, is that organisations would be able to reduce their tax burden through fuel/tariff switching rather than through efficiency improvements. As such, it is important for Government to consider whether the primary aim for this reform process is to reduce emissions or to increase energy efficiency. Although often complementary, these two goals are not the same and would suggest different policy approaches.

10. Do you believe that the CCA scheme (or any new scheme giving a discount on the CCL or on any new tax based on the model of the CCL) eligibility should only focus on industries needing protection from competitive disadvantage? If so, how should government determine which sectors are in need of protection?

No comment

11. Do you believe that the CCA scheme (or new scheme) eligibility should focus only on providing protection to those EIIs exposed to international competition and at risk of carbon leakage? If so, how should the government assess which CCA sectors are at risk of carbon leakage?

No comment

12. Do you believe that the targets set by the current CCA scheme are effective at incentivising energy efficiency? Do you believe that the current CCA scheme is at least as effective, or more effective, at incentivising energy efficiency than if participants paid the full current rates of CCL? How could CCAs be improved? Are there alternative mechanisms that may be more effective?

No comment

13. Do you agree that incentives could help drive additional investment in energy efficiency and carbon reduction? Please explain why you agree or disagree.

There is little doubt that a well-designed incentive scheme could help to support and drive energy efficiency in non-domestic buildings. As discussed above, it seems unlikely that simplification alone will be sufficient to create the scale of change that we need, and therefore an incentive scheme can and should form part of an effective policy package.

14. What is the best mechanism to deliver incentives for investment in energy efficiency and carbon reduction (e.g. tax reliefs, supplier obligations, grants, funding based on competitive bidding)? Are different approaches needed for different types of business? If so, which approaches work for which business types? What approaches should be avoided?

It is widely suggested that avoided costs provide a greater incentive for action than additional payments. As such, there seems to be a strong argument for a new incentive scheme to be centred around a tax relief rather than any of the other mechanisms suggested. However, without significant further analysis this remains a point of conjecture and we would suggest that considerable effort and focus is put into developing and comparing the effectiveness of different approaches as this reform process is taken forward.

In doing so, there are a few issues that need to be considered in relation to property when designing a new incentive scheme:

- For many buildings, it is the way in which they are operated rather than their physical attributes that has the largest impact on their energy usage. As such, an incentive scheme should support investment in operational improvements and not just physical measures.
- As noted above, with energy representing a relatively small proportion of total costs faced by building owners and occupiers, the financial value of an incentive that was proportional to an organisation's total CCL bill is likely to be quite small. As such, it would be essential for the incentive scheme to dovetail with the levers provided by the reporting and tax elements of the policy framework.
- If an incentive is to be based on a CCL rebate, it is unclear how this will work for (and incentivise) tenants who do not pay the bill. Linked to this is the question of whether landlords would be required to pass on the value of rebates to their tenants, and if so how this would be policed.

When discussing the design of a potential incentive with our members, there were a number of interesting ideas raised which would be worth considering as any scheme is developed:

- For buildings, could a scheme be designed that, like the FiTs regime, required buildings to meet a certain operational efficiency standard (for example, a minimum DEC rating) before they could access a discount?
- Alternatively, could undertaking operational ratings (such as DECs) be included as a measure eligible for the incentive rebate?
- More generally, could the incentive be used to raise ambition in other areas of the framework? For example, access to the incentive could be limited to those that publically disclosed a greater level of performance data, or undertook their ESOS audit to a higher standard
- Similarly, could the incentive be designed to encourage better measurement and reporting in smaller businesses?
- If the incentive was tied to the recommendations in an ESOS report, it would need significant MRV, since these reports are commissioned and signed off by the companies themselves and would otherwise be open to abuse. One way of helping to overcome this would be through a strong disclosure requirements and robust board sign-off
- While, for some, access to capital could otherwise provide a constraint, the presence of an incentive scheme could have the helpful effect of supporting an increase in the use of Energy Performance Contracting.

Finally, as discussed in more general terms above, whatever incentive scheme is eventually chosen, there should be clarity from the outset as to the value of the incentive, any plans to reduce it over time, and its overall longevity. The example of the Feed in Tariff was consistently cited by members during the consultation as an effective incentive that was hugely damaged by regular changes and its sudden (unexpected) cessation. Without some guarantee of longevity, the impact of an incentive scheme is likely to be reduced.

15. What impact would moving to a single tax have on the public sector and charities?

In the light of the current drive to reduce the costs associated with the public sector, it is presumably more important than ever that money is not being wasted through poor energy efficiency. The public sector (and charities) – like their business counterparts – are likely to have considerable scope for improvement in their energy efficiency. As such, it is reasonable that they should be provided with incentives (both sticks and carrots) that

encourage them to take up this potential. Since all but the smallest organisations pay the CCL, this could sensibly provide one of those incentives. Smaller organisations within these sectors could have the same mitigating measures put in place as are eventually applied to SME businesses, thus protecting them from disproportionate burden. For the public sector, in the light of budgetary constraints, it would be important to ensure schemes such as Salix are retained or even increased so that lack of finance did not become a barrier to investment in energy efficiency. Without such a scheme, the net result would be a worsening in public sector organisations' finances.
16. How should the merged tax be designed to improve its effectiveness in driving energy and carbon savings from the public sector and charities?
We see little reason why the answers to this questions should be substantively different to those provided in response to questions 6, 7 and 8 above.
17. Should a new reporting framework also require reporting by the public sector?
Yes. Currently large parts of the public sector are required to report under the CRC, and it would make sense for this to continue under the new regime. In fact, previous years' CRC data suggests that public sector organisations are amongst the largest users of energy in the UK, and therefore could have much to gain from improving their energy efficiency. Public sector buildings are subject to renovation targets under the Energy Efficiency Directive, and participation in a reporting framework would certainly support the achievement of these targets. It is also important to note that all but the smallest public buildings are currently required to have Display Energy Certificates (DECs). As such, it should be relatively straightforward for public sector organisations to make use of their DECs and the underpinning data to participate in a reporting, audit and incentive scheme. In fact, it is important to remember that DECs are a recognised compliance route for ESOS.