Improving energy performance through lenders (England & Wales)

UK Finance response to BEIS consultation

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UK Finance is the collective voice for the banking and finance industry. Representing more than 250 firms across the industry, we act to enhance competitiveness, support customers and facilitate innovation. We welcome the opportunity to respond to the consultation on improving energy performance through lenders, and the proposed regime of disclosures and targets which are intended to ensure lenders help householders in England and Wales to improve the energy performance of their homes.

General comments

The banking and finance sector is behind the UK's commitment to achieve net-zero carbon emissions by 2050. We agree the economic recovery from the coronavirus pandemic should align to net-zero targets and drive business ambition to ensure we reach net-zero goals. Mortgage lenders have a vital role in this and are well placed to support housing retrofit. Transition to net-zero should be fair and inclusive and not leave individuals or households with stranded assets that are difficult to improve.

Lenders' role

Improving the energy efficiency of homes is an important issue which lenders are committed to supporting as an industry and as individual firms. There are, however, concerns within the industry that disproportionately allocating responsibility to lenders for ensuring the energy efficiency of homes will not be effective and could lead to unintended consequences. Only around 40% of properties in England and Wales are mortgaged, and lenders have limited financial levers to counter the costs involved in improving energy efficiency. A voluntary system for lender involvement may be more effective in driving change than one with legal or regulatory implications.

Government and regulators should be mindful that, in practical terms, it is unlikely that energy efficiency measures will be put in place quickly so annual reporting by lenders is unlikely, overall, to see significant changes year-by-year.

If standards are mandated, then the regulatory regime must not conflict with other lender requirements or obligations to both the PRA and FCA, such as prudential lending accounting for risk management, and balancing fair customer outcomes in new and existing lending.

Mortgage lenders are increasingly offering incentives for green house purchase and retrofit. Mortgage availability/ cost is a reducing issue, and the primary problem is the cost of retrofit versus the energy savings. Solving this is not within the gift of lenders.

Consumers and funding

Increasing consumer awareness and demand will be key to stimulating home retrofit for improved energy and environmental performance. Consumers must accept and support actions, targets and regulations that encourage change without penalising those less able to comply.

Lenders can support the ambition to improve energy efficiency of homes through finance. We are keen to work with government and key stakeholders such as the Green Finance Institute to develop innovative funding approaches including blended public-private finance for home retrofit.

To underpin consumer demand, ongoing government support will be needed to ensure retrofit is economically attractive, using targeted grants and/ or loans. Support should be in place for the foreseeable future as short-lived schemes and interventions do not drive longer-term change.

If necessary, government could encourage action via changes to council tax or stamp duty, although this might be seen as penalising inaction, rather than rewarding action.

Availability

Government should scale-up the green retrofit market and supply chain sufficiently to meet the level of decarbonisation needed. This could include substantially increasing the number of PAS-certified and TrustMark registered suppliers, if they are to be the only means of delivering retrofits of recognised quality; reducing the cost of PAS-certification and TrustMark registration; and promoting and creating apprenticeship programmes to increase the skills-base.

Challenges and necessary steps

Only 50% of the UK's properties have an EPC. Urgent effort is needed to expand EPC coverage. A commitment to roll-out EPC ratings for all households by 2025 would be welcome and a necessary precursor to minimum performance targets. This would help ensure the EPC data register is fit-for-purpose and updated frequently (with service level agreements and APIs and other technical changes that mean lenders receive better data). It would also enable a more up-to-date reading of the energy efficiency profile of the housing stock. We suggest also that EPCs are provided free of charge, to encourage uptake and remove cost barriers for homeowners.

The standard of EPCs needs to improve, with more consistency across the market so that they become a better source of information on individual properties. Currently, differences in reports mean they are only a rough guide to energy efficiency. In the mid-to-long term, changes to the EPC regime could consider whether the right environmental impacts are being measured, or if a better way of judging the environmental impact of a building could be used.

If EPCs are required beyond home-selling (for remortgages/ product transfers) and have a financial implication, then increased risk of fraud should be addressed in the policy/ regulatory regime.

Unintended consequences

It will be important to ensure that any new regulatory requirements for energy performance in owner-occupied homes do not cause market distortion or unintended consequences that might trap owners in poorer performing properties or create a two-tier market where borrowers pay more but have less choice. New and newer-build properties are likely to have better energy performance; it could be much more difficult to bring older properties up to standard in a cost-effective way. A two-

tier market could develop if there is a perception that energy efficiency requirements are value-affecting. Government should engage closely with RICS on this, as lenders rely on independent valuers for their property valuations, and they are guided by RICS as their professional body.

Any regulatory requirements on lenders should not favour specific market segments – for example new entrants who could 'cherry pick' properties with positive energy efficiency ratings – or penalise those providing mortgages to people on lower incomes and in older and listed properties which cannot be improved cost effectively. A robust exemption policy needs to be in place to avoid this.

We also caution that there will need to be clear consumer information about appropriate measures and installations to improve energy efficiency in their particular property. Not all interventions will be suitable for all properties. The push for energy efficiency should not create other property risks, particularly in older properties that need ventilation, air circulation and porosity to "breathe".

Alignment with other requirements on disclosures of climate-related risk

The reporting of carbon exposures from mortgage books is an important step to evaluating risk and tackling emissions in the drive to net zero. There are other initiatives in this space, and we would question whether disclosure of EPCs alone is the best route to driving a net zero outcome.

There is a fundamental question about the approach of BEIS in proposing to directly regulate disclosures from the balance sheets of financial services firms. In this, the sector has looked to the Taskforce on Climate Related Financial Disclosures (TCFD) and the Government has published a roadmap to mandatory TCFD reporting. The FCA in policy statement PS 20/17 on climate related disclosures makes full reference to TCFD, which references scope 3 emissions, such as those from a lending book, and the Science Based Targets Initiative. In addition, the PRA in their Supervisory Statement SS3/19 set out their expectations regarding firms embedding consideration of the financial impact of climate risk into their governance and management arrangements, scenario analysis and disclosure of financial risk from climate change.

In addition, the Financial Reporting Council supports proposals from the IFRS Foundation to set up a Sustainability Standards Board and consider a standard for climate reporting first. BEIS should consider requirements on lenders for energy efficiency reporting within this wider framework.

Although the timeline for mandatory TCFD disclosures extends to 2025, most banks, building societies and insurance companies are required to provide a full TCFD disclosure by the end of 2021. Guidelines have been issued over the past year to provide further clarity on TCFD requirements and what is deemed necessary to achieve a baseline disclosure. Although not directly referenced, EPC data is a critical data source that will feed firms' modelling capabilities to disclose metrics and targets for the carbon emissions of mortgage portfolios.

An integrated, aligned and coordinated approach from government would support the industry in its disclosure requirements and goals. The financial services sector has consistently called for more coordination in the regulatory framework within which it operates. BEIS should consider energy efficiency disclosures and reporting within the wider regulatory reporting obligations of the sector.

UK-wide

The proposals should ensure a sustainable and inclusive transition to net-zero that benefits homeowners in England and Wales, and their mortgage lenders. More widely, there should be a

broadly consistent approach across the UK nations to maximise change, compliance and understanding. This will need constructive engagement among the UK and national governments.

Specific comments and responses to consultation questions

Chapter 1: Disclosure of portfolio energy performance data

***Question 1.* Do you agree with the principle of all lenders publicly disclosing information on the energy performance of their portfolios?**

Yes. Lenders agree with the disclosure of portfolio energy performance data. Some lenders are already taking steps to report this as part of wider commitments to addressing environmental concerns and are looking to support customers improve the energy efficiency of their homes.

Any disclosures come with significant flaws in the data available. Only 40% of properties in the UK are mortgaged. Only half of properties have EPCs, and many of those EPCs are out-of-date. To be beneficial, disclosure needs near-complete coverage of up-to-date EPCs.

Clarity is needed on the aim of disclosure, which should drive positive action and not penalise homeowners, potentially even making some properties unmortgageable.

EPC data could be part of regular regulatory reporting rather than publicly disclosed. Any requirements on lenders to disclose EPC data should dovetail with requirements to disclose carbon emissions in annual reports, to avoid duplication of costs and non-alignment of available data.

***Question 2*. Do you agree with the proposed EPC information lenders will be required to collect? If you disagree, please explain why.**

Yes. It is recognised as the best source of data available, but there are limitations and gaps in available EPC data. This should be taken into account when considering requirements on lenders.

There are concerns about the efficiency of lenders collecting and sharing EPC data when there is an accessible government database already in existence. There could be better ways of sharing information on this dataset between industry and government.

The EPC database only covers England and Wales. There should be consistent arrangements for Scotland and Northern Ireland, to avoid lenders needing parallel processes to cover these. The open data set does not currently include EPCs of mortgagors who have opted out of Open Data and may not include the most recent EPC on a property if a new EPC has been created since the Open Data was updated. It would be significantly more costly for lenders to retrieve individual EPCs from the register where no Open Data exists. Using Open Data should be an acceptable approach to disclosure, with relevant commentary to support it.

Some lenders have suggested that it would also be beneficial if EPCs were tagged with the Unique Property Reference Number (UPRN) as the current data can only be matched by address, which has its limitations. Similarly, linking EPC and Land Registry data would be helpful for matching.

Some lenders have concerns about the effectiveness of monitoring EIR as some households obtain energy from sources which cannot be accurately discounted in their net EIR outputs.

***Question 3.* Do you agree with the proposed disclosure information? If you think there is other information that would be useful to disclose that is not included in this proposal, or you do not agree with the proposal, please explain why.**

Most lenders agree with the proposed disclosure information in general but have some concerns about the disclosure of gross value of mortgage lending by EPC band over the reporting period (item 4) and the gross value of 'green' mortgage lending for energy performance improvement works by EPC bank over the reporting period (item 5).

On item 4, lenders have pointed out that they do not necessarily fund against specific properties where they provide finance for books of properties (i.e. buy-to-let or 'commercial' funding for rental properties). Including figures for the whole book when a firm lends against only a portion of it would lead to poor data. Further consideration of this would be helpful.

On item 4, some lenders have concerns about applying this to remortgages, product transfers or additional borrowing (i.e. lending which is not for home purchase) because of the costs and time involved, other lenders have suggested that not including this lending would give a misleading impression of relative lender performance. We would support further consideration of this.

Generally, lenders have suggested that age bands of properties should be included within reporting as this will have an impact on individual EPC ratings and a lender's overall portfolio.

On item 5, lenders are concerned there is no agreed industry definition of green lending or way of checking what lending is used for. Requirement to record this information and verify works will increase complexity and cost for lenders, brokers and customers and disrupt mortgage processes.

As a final point, lenders who securitise their lending books have questioned the commercial impact of publishing detailed information about their back book and whether this will cause additional issues with regulators who already require significant amounts of information.

Question 4. **Do you agree that the option to provide additional commentary alongside disclosures would be useful? If not, please explain why, including any alternative proposals.**

Yes. Lenders would support the option of providing additional commentary alongside disclosures, providing that this is at the discretion of individual firms. It would enable lenders to provide context for reporting such as age of portfolio, regional differences, and performance of market segments.

Question 5**. Do you agree with the proposal that all lenders, irrespective of market share, be required to publish energy performance data on their websites as well as on GOV.UK aligned to annual reporting deadlines? If not, please explain why.**

Yes. It will ensure a level playing field across the mortgage market. It would also ensure that all lenders consider how to drive forward good customer behaviour and prevent a situation where customers seeking to avoid action switch to lenders that are not encouraging action.

Question 6**. Do you agree with the proposal that government use the disclosure information to publish 'league tables' of lenders? If not, please explain why.**

No. Lenders generally disagree with this. We would want to understand the rationale for publishing a league table and what behaviour it aims to achieve. There is a serious concern that if lenders are judged by their league table position, then they will be criticised for a metric which is not within their direct control (i.e. what the energy rating of a property is and what steps have been taken to improve it). This may lead to negative unintended consequences if lenders withdraw from underperforming sectors of the market, leaving them underserved. This could negatively impact key sectors of the housing market which the government are keen to support, such as affordable or

low-cost housing as well as older and listed properties and specific groups of customers such as those on lower incomes or with less savings or equity.

***Question 7*. Do you agree that properties financed by a Buy-to-Let mortgage should be included in the scope of the policies proposed in this consultation? If not, please explain why, including any alternative suggestions.**

Yes. It may be more suitable for disclosures to be kept separate rather than consolidated due to the different nature of the market and policy measures. Furthermore, government should ensure that proposals for mortgage lenders to disclose energy efficiency in buy-to-let mortgaged properties are aligned to any requirements on landlords as many properties will be unmortgaged.

***Question 8*. Do you agree with the proposed trajectory to mandatory disclosure? If not, please outline the reasons why.**

Yes. Voluntary disclosure should precede any mandatory regime. Disclosure will require considerable time and resources to achieve because of need to implement process changes for data capture, monitoring and checking. 2023 is a short timescale for mandatory disclosure given that voluntary disclosure has not been implemented or embedded yet within the industry. A longer timescale for achieving this would be needed. Allowing more time would support testing and evaluation of voluntary disclosure. It would give the government time to improve the EPC data, which should be a prerequisite of mandatory disclosure. Government should set a timescale now for evaluation of voluntary disclosure and consultation on any move to mandatory disclosure.

***Question 9*. Do you agree with the proposal that disclosure information be subject to spot check audits proportional to the size of the lending portfolio? If not, please explain why, including any alternative proposals.**

The majority of lenders agree with this proposal, but there are some who argue that internal controls should be sufficient and that external audit is an unnecessary cost.

Chapter 2: Improving the energy performance of lenders' portfolios: target-based approach

***Question 10*. If applicable, is your organisation likely to sign up to a system of voluntary targets? If not, please outline the reasons why.**

There are mixed views on this. Some lenders might sign-up to voluntary targets and are already in the process of designing frameworks that include targets to improve the energy efficiency of properties and to support customers in achieving those. Other lenders are concerned, however, about agreeing to a voluntary system of targets while government support to achieve them remains uncertain and the flaws in the EPC system remain.

More broadly, there are concerns that the proposals represent a fundamentally different approach to owner-occupied property than that in Private Rental Sector. In the PRS, regulation places requirements to meet EPC thresholds on landlords directly, not via lenders. For owner-occupied property, government are not proposing direct requirements on homeowners, but to use lenders to seek to influence them. This is inefficient as only around 40% of residential property is mortgaged.

Additionally, although people may stay in their home for an average of around 18 years, the average life of a mortgage account with a lender is 5.4 years. The window of opportunity for a lender to influence a customer is relatively short and the assumption that lenders can influence customer behaviour in favour of energy performance retrofit may be incorrect.

The potential lending propositions outlined in the consultation are feasible but assume a willingness and financial ability in householders to increase secured borrowing to improve energy efficiency. This may not be the case, especially in current circumstances where the pandemic and related impacts are likely to make households cautious about significant spending.

There are concerns about borrowing to reduce energy consumption that are likely to affect consumer behaviour. There are customer groups who are less likely to be able, or willing, to finance home improvements. This include those who are already at the upper limits of their borrowing, such as first-time buyers, and those who will not own the property for long enough to realise the benefit of retrofitting (whether return on investment or increased property value).

In many instances, secured lending may not be the best or most appropriate option for a customer, and could be an expensive way to borrow given the length of repayment. Unsecured short-term lending, or the use of personal savings, may be more appropriate. Responsible lending rules require lenders to assess product suitability. Setting targets for secured lending ignores this. In addition, some lenders may not offer unsecured lending facilities. The value-add of energy efficiency improvements is not yet clear enough for consumers to make informed choices readily.

There are customer groups within the market where further borrowing, secured or otherwise, is unsuitable. Lenders have a duty of care to lend responsibly to all customers and there are higher-risk market segments that are particularly vulnerable, or where further borrowing is likely to be unsuitable. These customers may also not be eligible to access grant finance. They include:

- Expired interest-only mortgage products with outstanding capital to be repaid
- Lending into retirement (i.e. a reduced income)
- Mortgage prisoners
- Customer in arrears, with adverse credit or a poor credit history
- Leaseholders, including those affected by cladding issues and escalating ground rents
- Customers with high loan-to-income ratios or stretched affordability
- Higher loan-to-value customers, such as first time buyers
- Customer consolidating unsecured debts

It would penalise these customers via banking targets and potentially create a two-tier market, with better-off customers financially rewarded and already less well-off customers penalised. Some lenders have flagged the potential for homeowners to consider not increasing the energy efficiency of their home so that they can access any special support for poor performers.

Overall, lenders have the potential to influence homeowners, provide support, educational content and finance options, but ultimately any home improvements are dependent upon customer take-up rates and a cultural shift in behaviour amongst the population.

***Question 11*. Do you agree with our estimate that up to 80% of mortgaged stock would fall within scope during the target period? Please provide evidence where available.**

No. Many lenders think the estimate of 80% of mortgaged property coming into scope during the target period is optimistic. Although it might be possible, it would mean a significant change in approach that envisages homeowners remortgaging or taking a product transfer obtaining an EPC assessment as part of the process. This could be time consuming and costly.

Whether consumers would be willing to take action to retrofit their homes upon remortgage or product transfer remains a serious concern. The positive impact of them being included within the target period is likely overestimated compared to the costs of doing so. Taking an 80% optimistic estimate of properties in-scope against around 40% of properties under mortgage, suggests only a

third (maximum) of properties could be reached via this initiative. This again underlines the potential inefficiency of proposing to use lenders as consumer influencers.

***Question 12*. Do you agree the voluntary target should be set at a portfolio average of EPC Band C by 2030? If not, please outline the reasons why.**

There is no industry agreement on this. Some lenders support the target, albeit suggesting that it is broken down my age of stock to reflect lender portfolios, and that it is dependent on government incentives and support. Lenders who do not support the target argue that it is a blunt measure which could lead to market distortion as lenders cannot significantly influence their EPC profile other than by seeking to lend on better rated properties and rejecting lower rated properties.

Again, lenders have a key role to play in helping customers to understand how and when to improve their home, the associated costs and crucially to help them finance the work. Government should, however, recognise that lenders' ability to incentivise borrowers is limited and many simply will not want to borrow more to retrofit.

One lender has suggested that an EPC rating of Band D is a more realistic and achievable goal.

***Question 13*. Do you think a revised EPC should be required to demonstrate improvements in energy performance? If not, what alternatives should be explored?**

Yes, all EPC's should be maintained and updated regularly, and a revised EPC should be required. However, there are questions around the costs and industry capacity to achieve this.

An option could be to require retrofit trade bodies, local authorities or building control inspectors to carry out EPC assessment updates after improvement works. This would ensure customers who self-fund or do not have a mortgage also maintain an up-to-date EPC. This data would then need to be available to lenders to validate that energy efficiency work has been completed.

If post-improvement EPCs are required, then it is likely this cost would fall on the customer. If the requirement sat with lenders then there is a risk that not all customers secure a post-improvement EPC, as some will continue to borrow for green home improvements on standard lending products. Any costs that fall to consumers would have to be included within lender mortgage calculations.

In terms of potential alternatives to be explored, government should lay out the acceptable alternative solutions to recording SAP score/ EPC impacts, to support reporting and agree a framework for how these could be transferred between lenders. If TrustMark is the only alternative validation approach, then there would need to be robust processes and sufficient capacity in place to deal with the wide range of requests from lenders for this assessment.

***Question 14*. Do you agree that an assumed maximum spend for improvement works should be set at £10,000? If you do not agree, please specify what you believe would be the most appropriate level to set the threshold, providing evidence to support your views where possible.**

The benefit of setting a maximum spend for improvement works is unclear given the vagaries in likely costs in making improvements between different types of homes and different locations. A single cap across England and Wales is a blunt tool that might provide enough finance in some cases to improve an EPC rating but might disincentivise improvements being made in others.

We would also welcome clarity on how the £10,000 cap would fit with grants that the government makes available to private homeowners (£5,000 or up to £10,000 for low-income families). There

needs to be a much longer-term commitment by Government to subsidies, until the cost of installing energy efficient home improvements reduces significantly.

Consideration could be given to an alternative scale if shortfalls cannot be subsidised with grants, such as a percentage-based approach.

***Question 15*. Should spend from April 2021 onwards count towards the £10,000 assumed maximum spend on improvements? If you believe an alternative date would be more effective, please set out the reasons why.**

Lenders generally do not believe they have adequate information to comment on this question.

***Question 16*. What actions could the government take to incentivise the lenders to sign up to a voluntary target? Please provide evidence to support your answer where possible.**

There are mixed views here; suggestions from lenders include:

- Creating a central database of EPC ratings for all properties with central management of an exemptions process, personalised customer information, easier access to EPC ratings and further support for customers to improve their rating.

- Subsidised schemes like Help to Buy which would attract positive publicity and help customers feel comfortable they will get similar service.

- Introducing a capital benefit for lenders. There are currently no capital benefits to providing loan commitments to landlords or individual property owners with a positive EPC rating, or to support the improvement of the EPC rating linked to a property. This would make funding more feasible at a lower margin to support investment focussed on improving EPC ratings.

- The government could commit to further support and incentives for homeowners to make energy efficiency improvements.

- Costs are one of the biggest barriers to action and therefore cheaper borrowing interest rates would appeal to customers and incentivise them to make improvements. A provision of beneficial funding rates under a Term Funding Scheme would support this by enabling lenders to access cheaper costs of funds, with benefits passed on to customers. Currently banks providing preferential funding rates for green lending products are taking the financial impact of this funding, which is not a sustainable model for retrofit market stimulation. Alternatively, this could be delivered through meaningful capital relief for improved EPC properties to provide commercial benefit.

- The capital relief measure, above, could also risk two-tier lending if better performing properties are more likely to attract discounted rates. It could also benefit larger lenders who are more likely to be able to make use of such government funding.

- Ensuring sufficiently trained EPC assessors, robust EPC assessments/ infrastructure; and exempting properties that cannot be cost-effectively improved from reporting requirements.

***Question 17*. Do you agree government should consider the option of setting a mandatory improvement target, should insufficient progress be made under a voluntary scheme?**

Generally, mortgage lenders do not agree with this approach. Lenders have key role to play in helping customers understand the benefits of energy performance retrofit and providing financial solutions to achieve this. There are concerns about making lenders accountable for improving private homes as lender propositions alone cannot properly incentivise homeowners to make green retrofit improvements. Upgrading properties relies on a broader range of actions outside lenders' control including grants, green retrofit supply chain and grid decarbonisation.

There could be unintended consequences if a mandatory target sees lenders limit lending to customers with lower EPC properties, in turn limiting a customers' remortgaging options or creating mortgage prisoners, leaving those who most need help with higher mortgage costs.

***Question 18*. Do you agree with our proposed approach to the penalty regime? If not, please explain why, including any alternative proposals.**

Most lenders have said that penalties on lenders for failures outside of their control would be unfair and probably lead to poor market outcomes for consumers if lenders act to prevent this happening (for example, by not lending on properties with poor energy efficiency). Lenders should not be expected to encourage consumers to take on additional borrowing for energy efficiency works as it would make them the back-door enforcers of government policy.

Where lenders are supportive of penalties, they are concerned that they should be detrimental to low-income households, those with less savings or equity, lower value properties including low-cost home ownership. Penalty receipts must be invested in plans to improve EPC performance.

***Question 19.* What public tools could be used to calculate foregone emissions savings so that lenders can assess their own liabilities?**

More clarity is needed on what public tools are available, such as open source data.

***Question 20*. Do you agree that the money collected from penalties be used to fund energy performance improvements? Please provide evidence to support your answer.**

Yes - although lenders are not generally supportive of penalties.

***Question 21*. Do you think that only those lenders that are on trajectory to meet their target should benefit from these funds?**

No. Funds should be directed at retrofit improvements.

***Question 22.* Do you agree that lenders below a certain value or size threshold should benefit from certain derogations from a mandatory target? If so, what form should these take and how can we avoid creating any policy loopholes?**

No. Derogations from mandatory targets could be aimed at specific property types to avoid distorting the market by making it harder for some lenders to comply (for example, those whose have significant books of older properties).

***Question 23*: Do you agree with the proposed alternative option of a mandatory target of a portfolio average EPC Band C by 2030 from the start of the policy? If you disagree, please explain why, highlighting any alternative target you think would be appropriate.**

No, we think this would be premature. Testing of voluntary targets is needed first, so lenders can understand what action is effective in moving consumers towards more energy efficient properties.

Wider considerations

Question 24. **These policy proposals rely on the information provided by the EPC. Are there any impacts of data collection using EPCs that we have not considered? If so, how could these be managed effectively by lenders?**

The EPC database must be kept up-to-date and made available to lenders, with the frequency of data available for bulk download becoming more regular and frequent than it is currently. It would also be beneficial if EPCs are tagged with the Unique Property Reference Number (UPRN) and if EPC data were linked to Land Registry property identifiers.

Asking lenders to collect and store EPC data at each transaction is problematic (and duplicates the work of the EPC database). Many properties do not have EPCs and requiring them at remortgage or product transfer would be time consuming and slow the customer journey. This is especially the case as these processes are becoming more and more automated, including automatic valuations or desktop valuations which do not lend themselves to EPCs.

Question 25**. What are your views on the likely impacts of requiring an increase in the EPC coverage of portfolios on: a) lenders; b) consumers; and c) EPC assessors?**

a) Lenders

- There could be limited impact for lenders but this will depend on what they are asked to record. If lenders are required to collect EPC data for remorgages and product transfers this would add costs and delays to the consumer journey.

- If lenders must proactively collect EPC data for existing stock this could have a significant impact as there would be a cost in obtaining, recording, maintaining and renewing records.

- If the requirement to have an EPC in place for all lending was not enforced uniformly in the market, this could penalise lenders who look to take early action, having a particularly adverse impact in the intermediary market where speed and service are key.

- The ‘opportunity cost’ of delivering this policy could mean a curtailment of non-green initiatives and hampered ability to respond in other areas.

b) Consumers

- The immediate impact would be the additional costs for customers. Either a direct cost for the EPC or indirectly through product pricing or additional transaction fees.

- Customers might experience delays to their mortgage application and completion, either for a remortgage to a new lender, or a product transfer with an existing lender.

- Obtaining an EPC for product transfers is likely to increase complexity and delay transactions. In some instances, this may mean customers inadvertently transferring to standard variable rates which will adversely affect their monthly expenditure.

- An unforeseen outcome could be a less active remortgage market with less choice for consumers due to added costs and complexity within the application process.

- Consumers would face increased costs to improve lower rated properties.

c) EPC assessors

There is clearly the opportunity for an increased market for EPC assessors, however, lenders have strong concerns about the capacity of assessors to be able to provide EPC ratings for all properties in scope. If assessors cannot meet demand in the required timeframe this would cause disruption within the mortgage market, for lenders and for customers, as well as the possibility of fraud.

***Question 26*. How can we ensure the effective transition of data between lenders when consumers change mortgage providers?**

Lenders should not manage the transfer of EPC data between each other. Instead, the data should be stored centrally on an open-source database that is accessible to all lenders (or closed source if some information needed to remain confidential). We would be concerned about any other processes as they could add unnecessary friction in the mortgage process.

***Question 27*. Are there any additional ways in which government or lenders could raise consumer awareness of their EPC data and how to improve the energy performance of their homes?**

All parties involved in the property market have a duty to encourage homeowners to improve the energy performance of their property. An awareness of EPC data is part of that. Several lenders already seek to educate staff and customers about the benefits of improving the energy efficiency of their homes. We would support further such actions and similar activity amongst other parties in the property market (estate agents, surveyors, conveyancers, developers etc).

A government-backed information campaign could help raise awareness, especially if it resulted in a single or agreed set of information about how to improve energy efficiency, financing and long-term benefits. Additional funding from government for improvements would be beneficial as this would give strength to any consumer campaign.

***Question 28*. Are there any ways in which lenders could help to encourage the installation of smart meters in the homes of those to whom they lend?**

This should be the responsibility of energy providers and government, not mortgage lenders.

***Question 29*. Should works carried out to comply with these policies require that mortgagors choose a TrustMark approved provider or installer?**

Yes. A requirement for all energy efficiency home improvement suppliers to be TrustMark registered would provide lenders with quality assurances and reduce the risk of redress requirements falling on lenders, as well as providing consumers with assurance. However, there is currently only a limited number of TrustMark registered suppliers. Government support is needed to enable the TrustMark registered supplier base to grow sufficiently to meet likely demand.

***Question 30*. We understand that there are mortgagors who will not be able to self-fund or borrow. Do you have any evidence that indicates what proportion of the mortgage market these mortgagors represent? Please provide as much detail as you can.**

To answer this question accurately lenders would need to make recalculations on loan-to-value, loan-to-income, affordability and personal circumstances. As a result, lenders do not generally have evidence to share. One large lender has calculated that further borrowing of £10k would put

22% of their buy-to-let and 7% of their residential portfolio outside of current loan-to-value lending criteria, and they anticipate this would increase once other factors are taken into consideration.

***Question 31*. Do you agree that those mortgagors unable to self-fund or borrow to make energy performance improvements should be exempt from inclusion in a lender's improvement target?**

This cannot be answered simply. Whether or not someone is able to borrow will be based on affordability calculations and mortgage offers available to them and these can both change frequently, as well as vary between lenders based on their experience and risk appetite. If lenders did have improvement targets with exclusions then establishing who falls under these would be onerous, particularly for larger lenders with substantial back books.

We are unconvinced that exclusions are necessarily a positive step. Clearly, we would not want to see lenders unable to meet targets for improvement if those improvements are unavailable for good reasons. Nor would we want to see lending criteria designed to safeguard customers set aside to allow borrowing for energy efficiency. However, excluding large groups from lender targets could lead to those less well-off being left in less energy efficient properties. More insight is needed about mortgagors who are unable to self-fund or borrow before any exclusions are made.

***Question 32*. How do you think exemptions on the basis of affordability should be assessed?**

If lenders are to be given improvement targets with exemptions, then areas which could form the basis for exemptions on affordability grounds could include:

- Customers with high LTVs
- Properties where reaching EPC D or over would cost more than a set figure (£10k or £20k)
- Customers who have chosen not to improve their property and instead focus on other green efficiencies (e.g. a new electric car)

***Question 33*. What other methods of protecting fuel poor mortgagors should the government consider in designing its proposals? Please provide evidence to support your answer where possible.**

Lenders do not define which households are 'fuel poor'. The government would need to establish a definition and manage a central database of properties to be exempted under this category, as well as offering fuel poor households direct support.

***Question 34*. Do you support the idea of lenders recommending referrals to energy suppliers under a future ECO scheme?**

This does not fall naturally within lenders' remit. Lenders would need reassurance they are not recommending third party suppliers of which they have little knowledge or oversight. There are better-placed advocates than lenders for any future ECO scheme.

***Question 35*. Are there any impacts on the protected groups that we have not considered?**

Yes, further consideration is needed in relation to:

- Properties designed with particular people in mind (e.g. for disabled or older people) where any retrofit work is likely to have a greater negative impact on the homeowner's well-being.

- Vulnerable customers and low-income households could be disproportionately impacted if lender or product choice is limited without the means or borrowing to improve EPC rating.

- There is also the potential to impact on renters, who are more likely to be young and/ or vulnerable, and low income, as landlords might look to sell properties when faced with increased costs to improve EPC ratings.

- Consideration should also be given to awareness for vulnerable or non-digital customers of the impact/ of EPC ratings on their own financial well-being.

- It is not clear if lifetime mortgage borrowers been considered (i.e. older people). They may not have desire or motivation to improve energy efficiency of their homes.

- The rental market could be affected if landlords pass on costs to tenants or leave the market restricting choice for tenants. This would disproportionately impact vulnerable tenants, particularly at the cheaper end of the market.

***Question 36*. We wish to include leasehold properties in the scope of these proposals in order that their owners or tenants may benefit from energy improvement works. How do you think the government should act to ensure that leasehold properties with a mortgage are captured by these policies, while acknowledging the challenges that need to be overcome?**

Mortgage lenders agree that leasehold properties should be included. There are difficulties in assessing the energy performance of leasehold properties, and individual leaseholders have limited scope to improve them. The long-term responsibilities for leaseholders and building owners will need to be very clear within guidance and legislation so that improvements can be made without prohibitively high costs to leaseholders. The long-term effect of retrofitting products should be considered so that leaseholders are not responsible for future failures.

***Question 37*. How can we ensure that we protect groups such as first-time buyers from being disproportionately penalised?**

If mortgages are used to drive change in home energy performance then it is inevitable that there will be losers. This is a flaw with this approach which the government needs to consider. Targets for mortgage lenders could mean that first time buyers may find that they need higher deposits or face higher interest rates because of a lack of suitable housing stock and lender appetite.

Removing first time buyers from reporting has a limited effect as in a short period (2-, 3- or 5-years after their initial fixed term rate ends) lenders would need to include first time buyers in reporting and targets. There is a risk that first time buyers may find it difficult at the point of first product maturity to pass affordability assessments elsewhere and may be tied to their existing lender, with an inability to borrow more to fund green home improvements.

First-time buyers could be supported via provision of government backed guarantees for lending or by providing specific grants to support highly leveraged customers to take action.

***Question 38*. Are there other impacts these policies could have on mortgage processes that we have not considered? How do we ensure that intermediaries, such as brokers, have access to the information necessary to advise consumers?**

Brokers are a key part of the mortgage customer journey. Brokers need access to EPCs at the time of assessing mortgage applications. If lenders were to develop products varied by EPC band, this would need to be factored into search criteria on price comparison websites, lender mortgage calculators and broker sourcing systems.

For brokers to accurately advise customers on the best products for them, an EPC would be required in advance of the mortgage application. EPCs would need to be more widely available than currently, and more frequently updated. Education will be needed to prime customers for change. If EPCs are not available, there could be conduct challenges for intermediaries in recommending products before an EPC is in place. Brokers are ideally placed to inform clients about energy efficiency, and access to education/ solutions.

Question 39. **How can we ensure that our policies do not disincentivise lending to poor performing properties?**

This is a key concern for mortgage lenders. An unintended consequence could be that lending to poor performing properties is restricted. This could result in property devaluations and potentially negative equity. Targets on lenders which in effect put a new requirement on homeowners to improve EPC rating would affect the property value because of the cost of the work required. This drives up consumer costs and reduces their available capital to maintain or improve properties. It could also increase the number of lenders seeking to dispose of books of poor performing assets.

As a responsible industry, lenders would ensure that existing mortgage customers are able to take product transfers but even so this could create difficulties for those who wish to extend borrowing or move. We could see conduct risk emerge if this occurs, and potentially legal action being taken by consumers about the use of specific EPCs.

Question 40**. How might these policies impact on house prices and households' ability to borrow in the market? What could the government do to mitigate any unintended impacts on households?**

This is likely to be a significant unintended consequence of this policy. If properties are judged on their EPC rating it is inevitable that this will affect consumer behaviour which will, in turn, drive market views. To drive real change, energy efficiency needs to be reflected in property prices across the eco-system, from builders, to estate agents, to valuers, to lenders.

Some lenders have suggested government intervention is required to achieve widespread consideration for the value of home energy efficiency. Creating a sliding scale for stamp duty based on a property's EPC rating would incentivise the purchase of more efficient properties, which in turn may impact the property value. This could be further complemented by offering a stamp duty tax rebate if the EPC rating is improved. A system of government grants or guarantees for funding improvements would mitigate against a negative impact on households.

The policies could restrict a households' ability to borrow if affordability or lending limits are capped for higher EPC properties. For example, analysis by one lender shows that 30% of their customers with less than £10k borrowing affordability (EPC D-G) are categorised as constrained parents, despite only forming 10% of their customer base. Customers who may already struggle to access funding for retrofit may have their lending further restricted.

In the Dutch market it is common approach to allow adjusted LTV up to 106% (standard 100%) and adjusted Loan to income (LTI) affordability (up to 9k euros additional lending for green home

improvements). There is currently regulation in place in the UK around LTI limits that could be reviewed to support this type of approach.

***Question 41*. How might these policies negatively or positively impact on competition and lenders' ability to operate in the housing and wider market? What could the government do to mitigate any negative impacts?**

Lenders are concerned the policy could impact competition and lenders' ability to operate in the wider housing market. Targeting larger lenders only could result in an unfair advantage for new entrants or smaller lenders as they could provide funding without a requirement to ensure average EPC improvement over time. This would also mean housing stock is not improved.

Larger lenders are likely to have substantial portfolios of older, existing properties and long-standing customers. If lenders are penalised for legacy positions, or made the lending environment too challenging, then some lenders might exit the market or restrict funding against a portfolio of lower performing stock. This could reduce capital available for net-zero transition.

The policy could also impact a borrower's ability to raise funding from some lenders, in the event those lenders change their credit policies or housing market appetite. Borrowers might find it more difficult expensive to raise funding. This might restrict capital into the housing market, preventing the development of (greener) homes, or investment in improving existing stock.

The government can mitigate negative impacts on larger lenders by looking at differentiation within portfolios, ensuring that all lenders are included, and that lenders with large portfolios of poorer performing properties are rewarded if they improve, not penalised if they do not.

Conversely, some lenders have concerns about the impact on smaller/ regional lenders who may be less able to alter their EPC portfolio profile or absorb risks of a poor performing portfolio. Regionally based lenders might serve areas with a significant amount of lower standard housing or poorer customers who could suffer if they were served less well by the mortgage market.

Some lenders have also argued that these changes are likely to drive higher levels of innovation in the market for green lending products. Conversely, they may adversely impact competition if the costs associated with capability development and the incentives required to encourage homeowners to act are deemed too high to warrant market participation.

***Question 42*. What costs would compliance with these policies likely generate for lenders? Please provide an estimate of these costs where possible, including evidence to support your answer.**

There would be significant additional costs for lenders, running to several million pounds at least for larger lenders. Costs would include staff time, operating systems and process improvements, record management of EPC data, internal and external training, development of green finance products, marketing and advertising costs, funding costs associated with improving the EPC performance of portfolios, and auditing costs. There could also be less apparent costs such as slowness in the mortgage process. Ultimately these costs would be borne by consumers.

***Question 43*. Do you think a regulatory body should be responsible for the mandatory policies in this consultation? If so, what form do you think this body should take?**

Yes. It may be that the FCA could undertake this role, subject to further consideration.

Question 44. **Do you think that the government should introduce a requirement on lenders to check that privately rented properties comply with the Energy Efficiency (Private Rented Property) (England and Wales) Regulations 2015?**

No. Lenders should not be required to enforce or police landlord regulations, although they may include compliance checks within the mortgage application processes. Most privately rented properties are not subject to buy-to-let finance. If all renters are to be protected and all landlords to be made responsible then a different enforcement system is needed, perhaps via local councils.

Question 45**. Do you think it would be sensible for these proposals, for example annual disclosure of portfolio-wide EPC information, to be applied to smaller non-domestic buildings that require similar energy performance upgrades to homes?**

No response.

Question 46. **Should a fabric first approach be built into the preferred, voluntary, target option? If yes, how should such an approach best be implemented?**

No. Government should provide information and advice for consumers to inform their retrofit decisions. Using mortgage lenders to drive consumers towards certain decisions could be detrimental to improving the overall efficiency of housing. For example, homeowners could choose to fund a minor improvement now rather than a deeper costly retrofit later. To support fabric-first improvement, government should educate consumers and provide long-term retrofit funding.

Question 47**. What are your views on how we could tighten standards to drive greater carbon savings? Do you have views on introducing a dual metric, an alternative carbon target, or any other suggestions?**

There are already concerns about the timeline for implementing these policy changes among lenders. Developing and embedding a new system would be extremely challenging and confusing for consumers. Some lenders have suggested that ensuring that low carbon heating is adequately included and encouraged within the EPC system would be beneficial.

Contact

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