| Regulatory Policy Committee | **Opinion** | |
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| **Impact Assessment (IA)** | Private Rented Sector Regulations | |
| **Lead Department/Agency** | Department of Energy and Climate Change | |
| **Stage** | Final | |
| **IA number** | DECC0168 | |
| **Origin** | Domestic | |
| **Expected date of implementation** | SNR 9 | |
| **Date submitted to RPC** | 23 January 2015 | |
| **RPC Opinion date and reference** | 29 January 2015 | RPC14-DECC-2069(3) |
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| ***Departmental Assessment*** | | |
| **One-in, Two-out status** | **Zero Net Cost** | |
| **Estimate of the Equivalent Annual Net Cost to Business (EANCB)** | **N/A** | |
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| **RPC Overall Assessment** | **GREEN** | |

**RPC comments**

The IA is fit for purpose. The Department has provided sufficient evidence in its impact assessment to show that the benefits to business of the proposal are likely to outweigh its costs to business. The Committee, therefore, can confirm the proposal as an IN with Zero Net Cost.

The Department has provided an assessment of the overall level of uncertainty and associated risks, and justified the best estimates set out in the impact assessment. The RPC acknowledges that the Department has taken a proportionate approach and used the best information available in light of the level of uncertainty.

**Background (extracts from IA)**

**What is the problem under consideration? Why is government intervention necessary?**

*"A number of barriers prevent both households and businesses in the Private Rented Sector (PRS) from benefitting from cost-effective energy efficiency measures. These include split incentives - where landlords bear much of the upfront costs while many of the benefits accrue to tenants – landlord or tenant inertia, and imperfect information. Government intervention is required because energy efficiency across both the*

*domestic and non-domestic PRS has an important role in contributing cost-effectively to climate change and fuel poverty commitments. A number of existing policies partially overcome these barriers, particularly where tenancies are long; however, the current policy framework alone will not drive uptake of cost-effective measures in this sector."*

**What are the policy objectives and the intended effects?**

*"The policy intends to drive cost-effective energy efficiency improvements in the domestic and non-domestic PRS, which would not have occurred otherwise. These energy efficiency improvements will lead to: fewer greenhouse gas emissions, potential economic growth and employment, lower energy bills for businesses and households – including those deepest in fuel poverty, and lower overall energy demand. The policy will also lead to greater energy security, improved air quality, and improved health outcomes as a result of warmer homes."*

**Comments on the robustness of the OITO assessment**

The Department explains in its impact assessment that the proposal is regulatory and it is net beneficial to business (an 'IN' with 'Zero Net Cost'). The Department's assessment is consistent with the Better Regulation Framework Manual (paragraph 1.9.12). Based on the evidence presented, the appraisal appears to provide a reasonable assessment of the likely impacts.

**Comments on the robustness of the Small & Micro Business Assessment (SaMBA)**

The proposal increases the scope of regulation on business. A SaMBA, therefore, is required.

Non-domestic sector

The Department provides a breakdown of the ownership of properties in the non-domestic sector. Rented commercial property is owned mainly by UK institutions, overseas investors, collective investment schemes, UK Real Estate Investment Trusts, listed and unlisted property companies. The Department assumes that only a small fraction of commercial landlord businesses in the non-domestic sector are small and micro businesses. The Department has not been able to quantify this fraction due to the lack of available data and despite attempts to source evidence during consultation.

Domestic sector

The Department sets out in its impact assessment that there are 1.6 million landlords in the domestic sector. 78% of them own a single property each, and 17% own between two and four properties. The Department has assumed, therefore, that all landlords in the domestic sector are small and micro businesses.

Exemption and mitigation

The Department is not proposing to exempt small and micro businesses from the requirements of the proposal or mitigate its impact. It argues that, given the large proportion of small and micro businesses that make up the domestic sector, excluding these businesses would remove most of the intended benefits of the proposal. The Department goes on to explain that smaller businesses will not face a disproportionate cost as the proposal is designed to impose costs on a per-property basis. However, the Department could improve the impact assessment by explaining the assumption in more detail as certain costs may be fixed, regardless of the number of properties within a landlord's portfolio.

Based on the information provided on the impact of the proposal on small and micro business landlords in the domestic sector, and the approach to achieving the intended objectives of the proposal, the SaMBA is sufficient.

**Quality of the analysis and evidence presented in the IA**

The Department proposes measures to increase the uptake of energy efficiency measures in the private rented sector. It aims to achieve this in the following ways:

- From 1 April 2016, landlords of domestic properties will not be permitted to refuse unreasonably the requests of their tenants for consent to energy efficiency improvements. Financial support is available to ensure that landlords face no up-front costs, for example, the Green Deal, Energy Company Obligation (ECO), tenant's own funds, or national or local authority grants. This obligation applies to all domestic properties irrespective of their Energy Performance Certificate (EPC) rating.

- From 1 April 2018, landlords must bring the energy efficiency of all applicable privately rented properties in the domestic and non-domestic sectors up to a minimum EPC rating of 'E' provided this can be achieved with no up-front costs. Landlords should make these energy efficiency improvements at the time of all new lettings or tenancy renewals.

The Department estimates that the proposal will result in an overall direct net benefit to business of £94.8 million each year. These savings derive predominantly from reduced energy consumption and the associated reduction in energy bills in the non-domestic sector.

Domestic sector costs

The Department assumes that all tenants in the domestic sector are households. In order to qualify, energy efficiency improvements must not impose any upfront costs on landlords and will typically be financed via measures such as the Green Deal. Tenants will cover the installation costs as part of their energy bills. The Department estimates that these costs will be more than offset by a reduction in energy bills due to reduced energy consumption. On this basis, the Department estimates the proposal to be net beneficial to the tenant.

As tenants in the domestic sector are not businesses, costs to businesses (landlords) include Green Deal assessment costs, familiarisation costs, hidden costs and Green Deal loan repayments during void periods i.e. when the property is not occupied by tenants and costs have to be met by the landlord. Hidden costs – non-monetised costs due to time and inconvenience – are assumed to be 10% of installation costs and act effectively as an optimism bias adjustment in the Department's impact assessment. The Department estimates that landlords will bear 75% of the hidden costs. The Department estimates that the cost to business in the domestic sector will be £2.1 million each year.

Non-domestic sector costs

The Department estimates the cost to business in the non-domestic sector to be £55.9 million each year. The estimate includes familiarisation costs, Green Deal assessment costs, hidden costs and Green Deal repayments during void periods. The Department's estimate of the cost to business is higher than in the domestic sector because it also includes other costs associated with the physical installation and financing of energy efficient measures. In the non-domestic sector, these costs fall on business tenants and are included in the Department's EANCB calculation. In the domestic sector, the installation and financing costs fall on private tenants i.e. tenants that are not businesses. The Department has, therefore, not included these costs in its EANCB calculation.

Domestic and non-domestic sector benefits

The Department identifies reductions in energy bills as a consequence of the proposal in both the domestic and non-domestic sectors. However, savings in energy bills materialise as a direct benefit to businesses only in the non-domestic sector. In the domestic sector, the Department expects direct benefits to accrue only to private tenants, rather than to businesses,

DECC estimates the savings to business consumers will be approximately £153.6 million each year.

Counterfactual and calculation of the net benefits to business

The estimated uptake of energy efficient measures in the proposal and the counterfactual is subject to high levels of political, technological and economic uncertainty. The Department explains that the magnitude of the effects depends on several parameters, such as energy prices and other economic factors. The proposal has been assessed over a 52 year appraisal period. This timescale appears reasonable to capture the benefits of the proposal. Predictions and assumptions about technological advances and energy prices will also be subject to a related level of uncertainty. However, the Department has addressed this uncertainty in its impact assessment by providing specific sections on risks and uncertainties, as well as a sensitivity analysis with respect to ECO funding and energy prices.

The Department has used large-scale modelling based on a number of evidence-based assumptions and parameters to determine the estimates of the costs and benefits to business. The net benefit figures identified in this final stage impact assessment are significantly higher than the estimates in the consultation stage impact assessment. The new model that the Department has used allows for reinstallation of energy efficiency measures, increasing both costs and benefits, e.g. replacing energy efficient light bulbs or maintenance work that may be required on larger energy efficiency improvements. The net effect is an extension of the effective life of some energy efficiency improvements and an increase in the estimated net benefits.

Working in the opposite direction, the Department considered the effect of the proposal on house prices to be a direct benefit to businesses in its consultation stage impact assessment. However, the Department has reassessed the impact on house prices as an indirect pass-through benefit from tenants to landlords as a result of higher rents being charged now or in the future. As an indirect benefit to business, the Department has excluded it from its final stage EANCB calculation.

The Department has provided sufficient evidence and addressed the high level of uncertainty around the estimated net benefit to business of £94.8 million. On the basis of the evidence presented by the Department, the assessment that this regulatory proposal is likely to be net beneficial to business appears to be reasonable.

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| **Signed** | | **Michael Gibbons,** Chairman |