

Energy Company Obligation: Help to heat – April 2017 to September 2018

Department for Business, Energy and Industrial Strategy

RPC rating: fit for purpose

Description of proposal

The Energy Company Obligation (ECO) places obligations on larger energy suppliers to deliver energy efficiency measures to domestic premises in the UK. The current scheme is due to expire on 31 March 2017. The Government is proposing to replace the existing ECO commitments with a new, cheaper scheme, which will run for a period of five years up to March 2022. ECO is currently made up of the following three elements:

1. The Affordable Warmth (AW) obligation, whereby energy companies are required to install energy efficiency measures in low income households.
2. The Carbon Emissions Reduction Obligation (CERO) whereby energy companies must achieve a certain reduction in carbon emissions.
3. The Carbon Saving Communities Obligation (CSCO), which targets households in specified areas to improve energy efficiency standards.

The new scheme will have significantly altered administrative rules and eligibility. The main changes are that the AW obligation will be more focussed on households in or at risk of fuel poverty, the CERO will require a smaller reduction in emissions, and the CSCO will effectively be removed.

To ensure a smooth transition to the new scheme, there is an 18 month transition period for the new requirements, running from April 2017 to September 2018. This final stage IA covers the transition period. The Department intends to submit a further IA covering the subsequent period to April 2022.

Impacts of proposal

The IA explains that energy companies will incur the direct material and labour costs associated with the installation of energy efficiency measures, along with the scheme's administration costs. The current scheme costs energy companies £840 million each year (in 2015 prices). Under the new scheme, this is expected to fall to £620 million (in 2015 prices) each year. This is comprised of CERO delivery costs of

£160 million, Affordable Warmth costs of £380 million, and administration costs of £80 million.

The IA sets out a number of other monetised benefits including energy savings and increased comfort for consumers, increased air quality, and reduced carbon emissions. Overall, the Department estimates the net present value of the transition scheme to be £634 million. The Department has explained that there will be no direct benefits to energy suppliers from complying with the proposals.

The RPC verifies the estimated equivalent annual net direct cost to business (EANDCB) for the expiry of the current ECO scheme to be -£781 million and the EANDCB of the introduction of the transition scheme to be £576 million.

Both will be qualifying regulatory provisions that will score under the business impact target.

Quality of submission

Following the issue of the RPC opinion of 1 December 2016, the proposal has been revised by the Secretary of State for Business, Environment, and Industrial Strategy in relation to the Affordable Warmth element. The income threshold for eligibility for Affordable Warmth has been raised to bring more households within scope of the scheme. This revision, while making a very small adjustment to the NPV figure, does not change the overall cost of the scheme. The EANDCB figure is, therefore, unchanged.

The IA provides a thorough assessment of the proposed changes to the ECO scheme for the transition period. As requested at consultation stage, the Department has provided further evidence to support its estimates for the £5 million per annum reduction in administrative costs. The IA explains that this is due to the simplification of the scheme. The reduction has been estimated based on survey data from suppliers. The Department has also provided a helpful table setting out changes to its evidence base following the consultation.

The RPC, however, notes that the revised IA has removed large sections of text. While sufficient information remains for the RPC to validate the EANDCB figure, overall the IA does not provide a sufficiently detailed picture for such a complex proposal. For example, discussion of the key changes since the consultation; the transition to the new supplier obligation; and the inter-relationship with the Private Rented Sector regulations have been omitted.

ECO consists of a series of time-limited measures. For the purposes of scoring against the business impact target, the expiry of the current ECO scheme will score

as an OUT and the introduction of the 1½ year transitional scheme described in this impact assessment will count as a IN. The Department will submit a further IA covering the subsequent 3½ year period. This is likely to score as a substantial IN. The contribution of each element of ECO to the target will be scaled appropriately according to the duration of the scheme. The BIT scoring relevant to this IA is shown in Table 1 below.

Table 1 BIT scoring of ECO

Measure	EANDCB	BIT multiplier	BIT score
Expiry of existing scheme	- £781 million	5	- £3,905 million
New transitional scheme	£576 million	1.5	£864 million
Net BIT score	-	-	£3,041 million

As the proposal is of domestic origin, a small and micro business assessment (SaMBA) is required. The IA explains that all the businesses directly affected by the proposals are large energy suppliers with over 250,000 customers, supplying over 400GWh of electricity or 2,000GWh of gas per year. The scheme, therefore, does not impose any obligations on small and micro businesses. It is possible that in the future, a small business may grow large enough to become obligated – indeed, some did so during the lifetime of the previous scheme. However, the proposal includes a taper, whereby any obligation is introduced gradually. In addition, the IA explains that, due to the costs imposed on large energy suppliers, smaller suppliers should benefit indirectly from the proposals.

The IA could have been improved by including evidence of learning from the preceding ECO scheme more explicitly – though some of the consultation evidence clearly reflects consultees' experience of ECO.

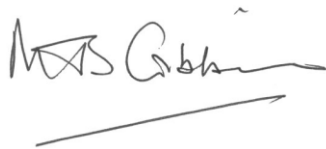
Departmental assessment

Classification	Qualifying regulatory provision (net OUT)
Equivalent annual net direct cost to business (EANDCB)	-£781 million OUT (expiry of existing ECO scheme) £576 million IN (transition period for new ECO scheme)

Business net present value	-£888 million (for the IN) ¹
Societal net present value	£638 million (for the IN) ¹

RPC assessment

Classification	Qualifying regulatory provision (net OUT)
EANDCB – RPC validated ²	-£781 million OUT (expiry of existing ECO scheme) £576 million IN (transition period for new ECO scheme)
Business Impact Target (BIT) Score ¹	-£3,041 million
Small and micro business assessment	Sufficient



Michael Gibbons CBE, Chairman

¹ Calculated over 1.5 years

² For reporting purposes, the RPC validates EANCB and BIT score figures to the nearest £100,000.