Regulatory Policy Committee

ECO3: improving consumer protection

Department for Business, Energy and Industrial Strategy

RPC rating: fit for purpose

Description of proposal

The Government propose an amendment to the current Energy Company Obligation (ECO3) delivery framework with an aim of improving the quality of installations and consumer protection standards of ECO3 measures. The proposal will introduce a new quality mark framework, using the existing *TrustMark* government-endorsed quality scheme, and a new set of technical standards, the Publicly Assessible Standards (PAS2035:2019).

Impacts of proposal

Businesses affected

Energy companies procure energy efficiency measures under ECO through delivery partners, who in turn sub-contract with installers across the supply chain. It is estimated that there are several hundred delivery partners working with energy companies, although some of the larger energy companies also have their own delivery arms providing specific energy efficiency products such as boilers and wall insulation. Delivery partners sub-contract by working with an estimated 2,300 installers across the local supply chain.

The proposal will run over the three-and-a-half-years life of the ECO3 scheme. The impact assessment (IA) identifies two main costs of the proposal, the cost to business of signing up to the *TrustMark* framework and, more significantly, increased delivery costs arising from the new PAS 2035:2019 technical requirements.

TrustMark framework

The TrustMark framework is designed to promote good practice by ensuring that companies are aware of their responsibilities to customers and the standards that energy efficiency measures must meet. The costs related to the *TrustMark* framework include: a one-off lodgement fee of £2,000 for scheme providers; an annual subscription charge of £40 per individual registered business; and the cost of lodging details of each of ECO measure on *TrustMark*'s ‘data warehouse’, at £8 per household. The IA estimates the total cost to business from the new *TrustMark* framework to be £3.14 million over the period of the scheme.

PAS 2035:2019 technical requirements

The IA describes the PAS 2035 framework as comprising the following steps: risk assessment; dwelling assessment, including ventilation; improvement option; advice; design; and monitoring & evaluation in accordance with PAS 2035. The Department explains that the cost impact of each these will depend on the level of risk, which will depend in turn on the complexity and/or scale of a project. The IA sets out three pathways, each with estimated delivery costs informed by industry (table 3, page 14). The Department's central assumption is that the new PAS 2035:2019 standards will increase delivery costs by an average of £350 per installation, reflecting additional assessment, design and evaluation requirements. An 18-month transitional period will run from the 1 Jan 2020 to 30 June 2021 to allow companies to begin working to the new PAS 2035:2019 framework.

Following consultation, the Government have made some changes to the proposal. These include two changes that significantly reduce the cost to business. First, an additional six-month transition scheme, which results in more of ECO3 being delivered at the previous, lower delivery price. Second, a 20 per cent uplift during the 18-month transition to the lifetime bill score for measures conforming to PAS 2035. This reduces costs because energy companies are able to achieve the same obligation with fewer measures.

The new PAS requirements are expected to increase costs to business by £59 million over the ECO period. This is markedly lower that the £198 million estimated at the consultation stage, primarily as a result of the changes described above which have reduced costs by approximately £48 million and £80 million, respectively. (The remaining £11 million difference reflecting updated actual data since consultation).

Benefits

The Government intend that the proposal will improve installation standards, particularly in respect of indoor air quality, and continue to professionalise the industry. Benefits are not monetised but are described qualitatively, such as helping to ensure installers implement an appropriate design specification and complete post installation checks, resulting in less remedial work.

Adding together the *TrustMark* and PAS costs results in an equivalent annual net direct cost to business (EANDCB) of £17.1 million over the three-and-a-half-year period (2016 prices; 2017 base year).

Quality of submission

The Department has provided a generally clear and well-structured impact assessment. The IA has been improved significantly since consultation stage and the RPC welcomes that the Department has taken account of its comments provided on the IA at that stage, notably through a revised approach to the counterfactual and a strengthening of the small and micro-business assessment (both explained below). The Department's analysis is sufficient for the RPC to be able to validate the EANDCB of £17.1 million. The measure is a qualifying regulatory provision that should be accounted against the business impact target.

Counterfactual

The Department's original consultation stage IA estimated the cost of the proposal against the counterfactual of the cost originally estimated in the October 2018 ECO3 final stage IA. This had the effect of significantly underestimating the cost of the proposal because this was largely offset by lower, updated ECO3 delivery prices and industry carryover. The Department now uses a correct counterfactual of the cost of delivering ECO3 prior to the change in cost from PAS2035:2019. The revised counterfactual has significantly altered the EANDCB compared to the consultation stage IAs. It was particularly welcome that the Department also revised the published consultation stage IA accordingly, providing greater transparency to consultees of the specific impact of the proposal.

Small and micro business assessment (SaMBA)

The Department has provided a good SaMBA. The IA includes a detailed description of the impacts of the proposal on small and micro businesses, including how they might be disproportionately affected. It explains why it would significantly compromise the policy objectives to exempt them but provides a full discussion of mitigation. The latter includes reference to policy changes following consultation, which should mitigate costs to businesses, including small businesses. The SaMBA could be strengthened further by quantifying the potential impact on a small business if, for example, it did not have access to retrofit co-ordinator skills in-house.

There are some additional areas where the IA could be strengthened, as outlined below.

- *Benefits and policy changes following consultation.* The IA would benefit from a much fuller discussion of the benefits of the proposal. This should include assessment of how the policy changes to reduce costs to business might reduce benefits, in particular the 20 per cent uplift that would appear to reduce the measures necessary for industry to meet its obligations under ECO. The reasoning behind the policy changes could also be brought out more in the IA.

- *Assumption of pathway B costs*. The Department sets out three pathways and explains why it takes pathway B for its central estimates. This appears to be a reasonable approach but the IA would be strengthened by a clearer explanation of the economies of scale in pathway C and how they arise.

- *Technical monitoring*. The estimated £350 additional cost per ECO measure excludes technical monitoring costs. The Department states that these costs are already accounted on the basis that technical monitoring is currently undertaken by *Ofgem*. Technical monitoring under PAS 2035 will replace *Ofgem*'s technical monitoring. The IA would benefit from clarifying who bears this cost currently and providing assurance that, if borne by *Ofgem*, this cost will not be passed to business under PAS 2035. If this cost is borne currently by business, the treatment in the present IA means that no saving to business should be accounted when this is no longer an *Ofgem* requirement.

- *Alternatives to regulation*. The inclusion of the section on page 9, following the RPC's comments on the consultation stage IA, is welcome but would be strengthened by further discussion on why these alternative options were not taken forward.

- *Supporting detail for cost calculations*. The IA would benefit from providing further details of the cost calculations, including the cost reductions from the policy changes following consultation. Should this be subject to commercial confidentiality, a fuller description of the methodology used to calculate the cost reductions would be helpful.

- *Monitoring and evaluation*. The IA would benefit significantly from including a formal plan explaining explicitly how the proposal will be monitored, enforced and evaluated through a post-implementation review.

Departmental assessment

Classification	Qualifying regulatory provision (IN)
Equivalent annual net direct cost to business (EANDCB)	£17.1 million
Business net present value	-£49.6 million
Societal net present value	-£49.6 million (benefits not monetised)

RPC assessment

Classification	Qualifying regulatory provision (IN)
EANDCB – RPC validated	Consultation stage: £0.9 million (original estimate) £56.0 million (final estimate) Final stage: £17.1 million (taking account of policy changes following consultation).
Business impact target score	£59.9 million
Small and micro business assessment	Sufficient

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