

Evaluation of the ECO: summary of findings

The Energy Company Obligation (ECO) launched in January 2013 alongside the Green Deal to replace CERT and Warm Front as the Government's flagship energy efficiency initiative. A year on, this independent evaluation investigates whether the initiative is meeting its aims and doing so within the predicted cost.

Key findings

- The first year of the ECO was delivered at an estimated annual cost of £1.54 billion, which is within the bounds of the final impact assessment of £1.30 billion (prior to the recent changes in the 'Future of the ECO' consultation).
- Despite slow initial progress, by the beginning of 2014, the ECO was delivering some measures at scale, particularly gas boilers and hard-to-treat cavity wall insulation.
- Progress on the HHCRO strand was on track to reach the March 2015 target, but progress on the CERO strand was somewhat short, and varied between energy suppliers.
- The original mix of primary measures under the CERO strand seems to be a design flaw which has caused activity to be skewed towards cheaper measures like hard-to-treat cavity wall insulation.
- The ECO has failed in its aim to support and develop a market for solid wall insulation, in part due to the scale of hard-to-treat cavity wall insulation. This has contributed to low take-up of Green Deal finance.
- Activity under the HHCRO / Affordable Warmth strand which targets low income households has so far focussed on replacing boilers in urban, gas-heated homes, leaving rural households disadvantaged. To date, the rural element of CSCo has not offset this bias.
- The ECO's very precise eligibility criteria and onerous reporting requirements have increased delivery costs, slowed down activity and hindered customer take-up.
- Transition to this scheme from CERT was initially slow due to full guidance being provided later than desired and delivery agents needing time to set up new systems to meet reporting requirements.
- The recently proposed changes to the ECO do not include a move to deemed savings for the re-introduced easy-to-treat measures, which would reduce the costs of assessment and reporting further.

We believe that the mismatch between DECC's expectations for ECO and the reality experienced in the first year of the policy demonstrates shortcomings in policy design at DECC. We recommend that DECC urgently finds ways to improve its capabilities to take account in policy design of the likely commercially-driven responses to its policy proposals by energy suppliers and companies in the housing retrofit supply chain.

Recommendations

The evaluation makes the following key short-term recommendations. Notably, the first recommendation does not feature in the recent DECC consultation on the future of the ECO:

- 1 Ofgem/DECC should set 'deemed savings' for each measure to reduce risk and simplify the proposition for customers
- 2 Show cross-government support for the initiative, to increase confidence within the supply chain
- 3 For solid wall insulation, introduce a minimum installations target into the ECO and increase Government cashback to customers
- 4 There should be ongoing collaboration between suppliers, Ofgem, DECC and installers to streamline the reporting requirements
- 5 Support the development of brokerage further though improved clarity of offers, separate CSCo rural lots and appropriate reporting to Ofgem.
- 6 Pre-verify householders' eligibility for HHCRO grants via the Department for Work and Pensions, to reduce the burden of paperwork and minimise data protection risks

Methodology

This evaluation involved a mixture of qualitative and quantitative surveys with the ECO supply chain, and detailed analysis of energy suppliers' data on costs and progress. Read the full report for a detailed summary of the methodology.

Analysis of costs and progress: key findings

Our analysis predicts a delivery cost of £1.54 billion per year with an estimated cost on bills for a dual fuel customer of £63. This is comparable with the value estimated by DECC in their final impact assessment. This is only an analysis of the ECO's first year, so it is difficult to draw long-term conclusions about delivery cost.

The contract approach for the delivery of the ECO does not appear to make a significant difference to the cost. For example, using brokerage, the total delivery cost would be slightly lower at £1.48 billion (N.B. that mandating brokerage would change this cost profile). The activity on brokerage has declined in recent months with the cost paid for measures dropping significantly. This is due to suppliers' progress on the HHCRO strand, and government announcements of changes with the 'future of the ECO' consultation.

CERO and the scale of HTTC activity

Whilst the delivery costs in 2013 were within the scale of the impact assessment, this was predominantly due to the amount of hard-to-treat cavity wall (HTTC) activity. 76% of all CERO measures in the dataset were HTTC installations. Our analysis suggests that the prices paid for these measures may in many cases be in excess of their market value. The cost of HTTC varies, with many potentially costing far less than the amount paid for delivery. Whilst these numbers do not reflect DECC's impact assessment predictions, they do reflect the market reality of the policy:

- Suppliers are choosing the cheaper of the two eligible CERO measures to discharge the obligation at least cost to their customers.
- The supply chain for cavity wall insulation was already well developed and adapting their business to HTTC was more straightforward than focussing on solid wall insulation.
- The size of the HTTC market is sufficient to allow all suppliers to avoid installing solid wall insulation in high volumes at a higher cost. (Note that the mix of measures varies by supplier.)

The approach of the recent Government consultation is to limit the HTTC market by reintroducing easy-to-treat cavity wall insulation and loft insulation as a primary measure under CERO. To reduce the cost of the obligation, the announcements also included a 33% reduction in CERO for the period to 2015 with a target for the 2015-2017 period reflecting this same level of activity.

The original Green Deal and ECO consultation document set out the Government's vision of a whole-house approach to energy efficiency where a household installed multiple measures as a package. Our analysis found that, in reality, 18% of measures were installed as part of a package, while the other 82% were installed on their own.

Solid wall insulation and the impact on the Green Deal

The encouraging costs of delivery mask the ECO's failure to support the supply chain for solid wall insulation. The number of solid wall insulation installations (just under 27,518 at the end of December 2013) is significantly short of that required to meet the Government's original aspirations for 1.2 to 1.3 million installations by 2020, or 175,000 by March 2015.

The level of funding available for solid wall insulation is not enough to enable installation at no upfront cost, even when Green Deal finance is added to an ECO grant, making this still an unattractive (or impossible) option for householders who want it. Furthermore, the size of the HTTC market meant that suppliers did not need to explore the price point required to encourage take up of solid wall insulation.

In response to the above issues, DECC's 'future of the ECO' consultation includes:

- A minimum target of 100,000 solid walls by 2017
- Higher cashbacks of £4,000 per customer for solid wall insulation (although this cannot be used in conjunction with ECO funding)

The minimum target for solid walls of 100,000 is likely to be predominantly achieved through direct contractual relationships with RSLs and local authorities. Our interviews suggested that several suppliers are seeking to develop these relationships, with CSCo area-based schemes seen as a good route to market. It is also worth noting that this proposed target (per year) is lower than the 82,000 houses that received solid wall insulation in 2012, before the ECO.

The proposed cashbacks are likely to make solid wall insulation a more attractive proposition for owner occupiers, particularly mid-terrace properties where the installed costs are lower and the level of subsidy (in this case) is no longer defined by the measure's savings. However, the total size of the funding pot and longevity of the cashback offer is unclear, particularly how many solid wall jobs the Government plan to fund by cashback over the next year and if funding will continue beyond that.

Affordable Warmth and rural households

Our analysis of distribution of measures against the English, Welsh and Scottish indices of multiple deprivation (specifically, income deprivation) found that, in general, proportionally more households in the most deprived areas are receiving measures, when measures from all the ECO strands are added together. This is a success story, showing that the policy is more progressive overall than CERT was.

Our analysis of installations by heating fuel and rurality show that current activity is heavily skewed towards urban areas and homes heated by gas. For example, 99% of HHCRO delivery has been in homes heated by gas with 70% of the measures being gas boiler replacements.

Across Great Britain, urban areas have benefited significantly more than rural areas, with rural properties making up only 7.5% of all properties receiving measures to date. The rural safeguard element of CSCo was meant to ensure that vulnerable rural households were able to access funding. At present it appears that this aspect of the ECO is failing. A lack of guidance on the geographical location of qualifying rural areas has been a factor in hampering progress.

Recommendations

1. Ofgem/DECC should set 'deemed savings' for each measure to reduce risk and simplify the proposition for customers

Based on feedback we have received, we believe a 10-15% cost reduction would be achieved if measures' savings were deemed in advance. To provide confidence that the customer is being offered the appropriate measure and allow compatibility with Green Deal Finance, the customer could still be given an assessment using the RdSAP and the EPC framework. This would provide a number of benefits, while removing the additional reporting burden associated with the current approach. The recent changes to the ECO notably do not include deemed savings, even for low cost measures like loft and standard cavity wall insulation (where the total cost of assessment and reporting may in some cases exceed that of the measure).

2. Show cross-government support for the initiative, to increase confidence within the supply chain

The Government's recent review of "green taxes" highlights a lack of cross-government and cross-party support for sustainable energy policy. Energy suppliers expressed a desire for a longer-term vision for the retrofit of the UK housing stock.

3. For solid wall insulation, introduce a minimum installations target into the ECO and increase Government cashback to customers

The recent changes to the ECO include a proposed minimum target for treating the equivalent of 100,000 solid walled properties by March 2017. As independent author of this report, CSE believes this minimum to be significantly lower than that required to develop a meaningful level of solid wall activity - one that stimulates a market for solid wall insulation in the non-social housing sector, and meets our carbon budgets.

4. There should be further collaboration between suppliers, Ofgem, DECC and installers to streamline the reporting requirements

There is currently a working group with members from energy suppliers, installers, Ofgem and DECC, which aims to identify ways to improve the reporting process for the supply chain. This group should work towards implementing the agreements to standardise practice, and review the forthcoming changes that are currently under consultation.

5. Support the development of the brokerage market further

Whilst our analysis did not find industry-wide support for the mandatory use of brokerage, there was a general level of support for the brokerage market as a route to delivery. There are a number of improvements that would help develop this: further clarity of the mix of measures in a lot; listing CSCo rural lots separately; and contracts that enable the delivery of the necessary reporting to Ofgem.

6. Pre-verify householders' eligibility for HHCRO grants via the Department for Work and Pensions

Under the ECO, the Energy Saving Advice Service (ESAS, run by the Energy Saving Trust) provides suppliers with details of consumers who have declared their eligibility and had this confirmed by DWP. ESAS directly refers customers to suppliers. We would recommend opening this referral market up to competition through other Green Deal Providers. In the next phase of the ECO, enabling pre-verification of Affordable Warmth customers through a system that is accessible to the supply chain is a fundamental necessity. This would reduce reporting requirements, minimise data protection risks and reduce administration costs.

This independent evaluation was carried out by the Centre for Sustainable Energy, led by Ian Preston and commissioned by Energy UK.



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