The Green Deal and Energy Company Obligation
Response by the Council of Mortgage Lenders
to the Department of Energy and Climate Change consultation

Introduction

1. The CML is the representative trade body for the first charge residential mortgage lending industry, which includes banks, building societies and specialist lenders. Our 111 members currently hold around 95% of the assets of the UK mortgage market. In addition to lending for home-ownership, the CML’s members also lend to support the social housing and private rental markets.

2. We welcome the opportunity to respond to the Department of Energy and Climate Change (DECC) consultation. Given that a number of the questions extend beyond the direct interests of our members, we are focusing on those areas that will have the most impact on our members and their customers.

3. We are keen to work with DECC to implement a solution that is practicable for our members and their customers.

Key points

4. We support government’s policy intention to improve the energy efficiency of property in the UK. However, we do not believe that focus on the Green Deal should be at the expense of other methods or finance options.

5. The consultation paper is very wide ranging and government is seeking to address a number of issues in a matter of months before launch. Our members’ recent experiences with the Feed-in-tariffs have reduced the mortgage industry’s confidence in government’s ability to implement a scheme such as the Green Deal, particularly within such a challenging timetable. It is vital that the exploration of important details, such as the Green Deal’s interaction with the Consumer Credit Act (CCA) and consumers’ credit files, is not compromised. We are concerned that the detail around the CCA implications has still to be fully considered by government, particularly where a new purchaser/tenant takes over the Green Deal liability.

6. Considering some of the proposals within this consultation document, we remain concerned that the Green Deal poses risk of detriment to mortgage lenders and their appointed agents, as well as current homeowners and prospective borrowers.

7. The term ‘Golden Rule’ is a misnomer, has the potential to mislead consumers and we believe it should not be used in any consumer facing information. The savings resulting from a Green Deal installation cannot be guaranteed to pay for a known liability. If the savings are not realised, this could have implications on household finances, including the ability to meet mortgage payments.

8. Disclosure of an existing Green Deal will be required by lenders from a remortgage perspective. And we do not agree that lenders should be carved out of the formal consents process for new Green Deals. Although the type of installation may in itself not require a lender’s consent, the fact that a charge will effectively reside with the property and become the lender’s responsibility when a property is in its possession may necessitate it in high cost or complex installations. We are keen to work with government in developing some broad guidelines on the circumstances when lenders will need to give consent and in what format.

9. This could instead be covered off in lenders’ mortgage deeds, but existing terms and conditions may not be sufficient to cover the unique nature of the Green Deal charge. If lenders were to introduce terms and conditions requiring consent of a Green Deal installation, this would
only be possible on mortgages yet to be underwritten and both consumers and Green Deal providers would need to be aware of individual lenders’ requirements.

10. Without this form of disclosure, the impacts on valuation and saleability are likely to remain unknown until the Green Deal has launched and bedded down. Valuations are only likely to be influenced if consumer understanding of a Green Deal installation’s efficacy has been proven or otherwise. Valuers will need to easily obtain this information and have the Green Deal disclosed to them at an early enough stage in the valuation process. Saleability may be impacted if potential buyers are sceptical of the installation’s benefits or request that the Green Deal plan be redeemed early by the incumbent.

11. If these issues are not considered carefully by government, the presence of a Green Deal plan may necessitate its redemption before the property is sold, or push down sale prices.

**Consumer protection and the ‘Golden Rule’**

12. We support the notion that a Green Deal installation should be able to pay for itself over its lifespan through energy bill savings. However, we believe that is potentially dangerous for government to both propagate the notion of a ‘Golden Rule’ and allow providers to use it in consumer facing literature, however heavily caveated. It cannot be described as such as there is no guarantee that the periodic Green Deal charge will be paid for by greater energy bill savings.

13. If customers misunderstand the limitations of the ‘Golden Rule’ or are led to believe that it is a de facto guarantee, we believe there is a significant potential for detriment to consumers, particularly those in vulnerable groups. We note that government does not believe that financially vulnerable homeowners will be able to obtain a Green Deal financed installation due to low fuel consumption. But government must avoid confusing financial difficulty with other forms of vulnerability - such as those suffering from mental health issues or the elderly. Appropriate safeguards in the sales process should be introduced for such groups.

14. The role of advice and the accreditation of installers will play an important role here, and we would hope that the Green Deal accreditation regime will signal an improvement on what our members and their customers have encountered on the Feed-in-tariffs. Government cannot afford to sacrifice consumer protection for the sake of promoting ‘maximum uptake’. We would urge that the use of cold calling and door step selling is either prohibited or subject to clearly defined safeguards.

15. We also believe that there is merit in requiring assessors to fully understand the nature and make-up of residential properties (e.g. such as a chartered surveyor), rather than using broadbrush estimates and metrics, which will be particularly important in calculating the energy efficiency of second-hand homes.

16. Irrespective of whether other methods of finance are discussed, the nature of the Green Deal finance will need to be clearly explained to potential customers. The DECC consultation paper references a “fixed rate interest deal […] possibly with an annual rise in instalments”. This would need to be explained very carefully to a consumer considering most homeowners existing knowledge of fixed rate loans.

17. We would also question the scope of advice in the selling process. Although this should naturally focus on the type of installation and associated energy saving, we believe that there is a risk of consumers being advised or persuaded to take out a Green Deal plan when this may not be the most appropriate method of finance. We believe that assessors should be able (from competency and regulatory standpoints) to advise on other forms of finance, including a further advance or loan.

18. We welcome the CCA protections, but early clarification is needed on how the Green Deal charge would be reflected on a customer’s credit file, particularly in the case of new buyers or tenants taking over a charge. It is vital that they are afforded proper protections and we are concerned that this has not yet been fully thought through by government. It is also important that early repayment charges are not gold plated, thereby preventing sellers with a Green Deal from paying off the finance. As outlined in paragraph 37, below, this early repayment may become a
condition of sale and potential barriers should therefore be avoided. This kind of detail will need to be fully developed and clearly communicated to homeowners in advance of the Green Deal launch.

**Mortgage affordability**

19. Mortgage lenders are governed by Financial Services Authority (FSA) rules on responsible lending outlined in chapter 11 of the Mortgage Conduct of Business (MCOB). The FSA’s most recent Mortgage Market Review paper, CP11/31, proposes strengthening these rules considerably.

20. Although we agree that the EPC calculations will be a reasonable proxy of how effective a Green Deal installation will be in paying down the finance, this cannot be taken as a guarantee. When undertaking affordability assessments on customers wishing to buy a property or remortgage where a Green Deal installation is present, lenders will need to understand that a Green Deal charge exists and the method by which it is being discharged (e.g. savings from the energy bill or the customer’s own finances). They may choose to obtain detailed figures from the existing or prospective homeowner rather than relying on government’s confidence in the ‘Golden Rule’.

21. And although the Green Deal instalments are likely to be relatively small for the time being given the current technological landscape for energy efficiency upgrades, they may adversely impact borderline mortgage applications or the amount advanced. In any event, charges stretching over a number of years will need to be looked at particularly closely.

**Consent and disclosure**

22. Given the regulatory importance in understanding borrowers’ expenditure, it is likely that lenders will need to give consent before particular Green Deal installations take place (i.e. existing lending) and disclosure before lending against a property where a Green Deal installation/plan is already in place (i.e. new lending, remortgages etc).

23. We support the principle of disclosure arising as part of the conveyancing process and we will be considering amendments to the CML Lenders’ Handbook in due course.

24. We are disappointed that government has opted to exclude mortgage lenders from the chain of parties that are likely to require consent. For at least some installations, a first charge lender will need to understand the appropriateness of the works, installation quality, listed buildings consents, building regulations, conservation areas and the impact on any new home warranty.

25. While it may be technically correct to state that the “Green Deal finance is not secured against the property”, it is likely to have a similar impact to a charge that is. This is because a local land charge will be registered, the liability for repayment will rest with the occupier (and owner where different), is part of a priority debt and can only be escaped by repayment of the finance. Furthermore, even if that charge was after a mortgage lender’s first charge, it would effectively take priority over the lender’s charge as it will not be overreached by a first charge lender selling in possession.

26. In the context of private landlords and freeholders, the consultation paper states that by “requiring written confirmation from the property owner, [government is] ensuring that, even if that person is not the bill payer or the customer when the Green Deal is taken out, they are aware that they could be responsible for paying the charge and bound by the terms of the plan in the future”. We agree with this principle.

27. Potentially, the lender will have to repay the capital (which would be added to the borrowers debt and could increase/create a loss to the lender) in the event that the lender has had to discount the sale price for the amount of the green deal financial plan or the lender has had to pay the green deal loan as a condition on sale. Paying off the Green Deal charge may impact on mortgage indemnity guarantee claims and may not be accounted for in residential mortgage-backed security transactions or securitisations.

28. Mortgage lenders will also need to know about a Green Deal installation to inform the asset managers they appoint or, potentially, a residing tenant where a Law of Property Act Receiver is acting as an agent of the borrower in default.
29. We appreciate that lenders could prescribe consent to a Green Deal installation as part of their terms and conditions, but lenders existing terms and conditions may not cover this given the uniqueness of the Green Deal charge and because it is not a charge against the property (although, as outlined above, it exhibits a number of similar characteristics). If terms and conditions do not cover this, lenders cannot retrospectively amend them on loans already advanced.

30. Even if terms and conditions did allow, consumers and providers may not be aware of each lender’s requirements. If consent was not sought from a mortgage lender as per the mortgage deeds’ terms and conditions, this would risk putting both the Green Deal plan and mortgage at risk.

31. We would therefore argue that mortgage lenders should need to give their consent, which should be requested in a broadly uniform form and that this should be communicated to consumers and providers alike. However, we recognise that it may be inappropriate to require lender consent in all instances, including lower value installations or shorter term Green Deal finance. We are keen to work with government to establish some framework criteria on when lender consent will be required and how this communicated to providers and consumers.

32. Lenders will also require disclosure of a Green Deal in the event of considering a further advance or a remortgage against a property. Again, this is likely to be dependent on some broad value/technology driven parameters, which we are happy to work with government in developing.

33. In specific answer to question 37, we would argue that individuals becoming party to a mortgage (i.e. in transfer of equity cases) should be made aware of Green Deal plans.

Saleability

34. We believe that there should be a straightforward mechanism allowing prospective buyers and tenants to understand how effective an existing Green Deal installation is proving in paying down the charge, and under what circumstances. Clearly data protection obligations will make this difficult on a property-by-property basis.

35. If a Green Deal installation is not proving as efficient (or even if it is proving more effective) as the original assessment and EPC disclosure envisaged, it is important that the process enables potential buyers to be made aware.

36. If this information is not made available, prospective buyers in particular may not feel comfortable taking on a liability spread over potentially several years. As a result, saleability of mortgaged properties could be compromised.

37. It is possible that an existing Green Deal could be considered a restriction which, at worst, may affect mortgageability. For this reason, and the fact that it normally happens when there is a local land charge (which government is considering for the Green Deal), it may become a requirement for Green Deal plans to be repaid at the point of sale. This process should be made as efficient and streamlined as possible, with proportionate early repayment charges.

38. We believe that prospective buyers should also be made aware of whether there has been any event requiring early repayment of the charge.

Valuations

39. It is important to recognise that mortgage lenders look at the market value of property; that is the value to be obtained between willing buyer and willing seller in an arms length transaction after proper marketing wherein parties act knowledgeable, prudently and without compulsion. At the moment, the impact of energy conservation measures on property value remains unknown. Installations with Green Deal finance are likely to follow suit unless Green Deal installations were to prove particularly effective or ineffective in paying down the charge.

40. There must be a mechanism in place to enable valuers to understand the presence of a Green Deal installation at an early stage to best inform valuations. The EPC will not be available at the point of valuation, so government will need to consider whether an additional part of the process is required.
41. Valuers will also need to understand the efficacy of particular installations in paying down the Green Deal charge. We understand that government has no strong appetite for disclosing this at an individual property level. But government will need to consider how valuers become aware of this over time.

42. The residential property market remains fragile. If a potential buyer is looking at two similar properties, one with a Green Deal installation and finance attached to it and one without, any complications associated with the Green Deal (borne out of misunderstanding or experience) may negatively impact the ‘improved’ property.

43. We would be interested to know whether government intends to adopt the financing framework proposed under the Green Deal for other improvements to offset climate change (e.g. on site flood defences). The cumulative effect of these particular financing arrangements may become more significant for valuers and lenders alike.

Managing properties in possession

44. It does not appear that government has yet fully considered the complexities that could result from a mortgage lender (or any other party) taking possession of a vacant property.

45. Although the draft statutory instrument proposes that a mortgagee in possession will generally not be liable for the Green Deal charge, government must ensure that this is borne out in practice. The vast majority (around 90%) of properties taken into possession are currently sold at a shortfall. Any Green Deal charge paid out by the lender is therefore likely to be added to the borrower’s shortfall debt. Although this can be pursued for up to six years [FSA MCOB 13.6.4R(2)], full recovery may not always be possible. Legal owners should therefore be responsible for both disbursement and the liability of the finance.

46. Without consent and disclosure, it will be particularly difficult for a lender in possession to understand what might be expected of them and/or repair poorly maintained equipment.

47. Similarly, if a lender takes possession of a property with a Green Deal installation/plan that is subject to dispute, how does the lender interact with this? It is also unclear how the Green Deal installation/plan will be managed in the event of abandonment.

Buy-to-let (BTL)

48. We support the proposal that both the owner (i.e. landlord) and energy bill payer (i.e. tenant) should be required to give consent to Green Deal installations on BTL properties. But with legislation outlawing the letting of F and G rated properties by 2018, it is important that government introduces mechanisms in the consents process to better enable upgrades to take place on these properties. Failure to do so could have implications for lenders with exposure to BTL-mortgaged F and G rated properties.

49. To discuss this response in more detail, please contact Nick Wood (nick.wood@cml.org.uk; 020 7438 8933).

17 January 2012