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Minimum Energy Efficiency Standards – thoughts on the consultation proposals

28 July 2014

This is a very long article. I have therefore prepared a PDF version of it, to make it easier to read and print out.

PDF version of this article

Last week, DECC issued two consultation documents on Minimum Energy Efficiency Standards (which I shall call MEES although I do not know whether that is going to become its accepted acronym). One document relates to domestic properties and the other to non-domestic properties. This article deals only with non-domestic properties, as I know nothing about MEES in the context of domestic properties. I have spotted that the consultation paper about domestic properties is half as long again as the one about non-domestic properties, which suggests there are more complications to be accommodated. In the interests of my sanity, I have not yet even looked at it.

Link to consultation paper on non-domestic properties

Link to consultation paper on domestic properties

The purpose of this article

The purpose of this article is to comment on DECC's consultation paper on non-domestic properties, to inform discussions about the proposals and to provide ideas that readers can incorporate into their consultation responses.

The consultation period, at six weeks, is ridiculously short. Almost one week has already passed and the majority of people affected are not aware of the consultation, let alone the details of what is proposed. Moreover the six weeks exactly spans the summer holidays, when few committees meet and no training events of any kind are scheduled.

I have written an article about the non-domestic consultation for Estates Gazette but that will not appear until the issue of 9 August 2014.

I have been told that the reason for the speed is to ensure that the regulations themselves can be made before Government closes down for the election in September 2015. I still think that a six week consultation period that exactly spans the summer holiday period is derisory. It gives the unfortunate impression that the Government is consulting because it has to, not because it wants to obtain ideas.

The purpose of the consultations

The purpose of the consultations is to enable DECC to finalise the regulations dealing with MEES, which the Secretary of State is under a duty to make no later than April 2018, according to section 49 Energy Act 2011. (This section is not yet in force; I imagine that the intention is to bring it into force at the same time as the regulations are made.) The draft regulations apparently exist but have not yet been made public. This is a bit of a nuisance as so far we have an incomplete picture of what is being proposed. Some of the issues are addressed in the text of the consultation paper but there are some issues that can only be understood by reference to the text of the regulations themselves.

Stakeholder working groups

This is not the first time that DECC has sought guidance from the property industry. As mentioned in paragraph 12 of the consultation paper's executive summary, in February 2013 DECC gathered together two working groups of stakeholder representatives – one for domestic properties and the other for non-domestic properties – and asked them to consider various issues related to MEES. I was a member of the non-domestic properties working group. Our role was effectively to devise the questions for this forthcoming consultation, and to suggest possible solutions.

The report of the non-domestic working group is now available on the Government's website at this link:

https://www.gov.uk/government/publications/non-domestic-private-rented-sector-regulations-working-group-report-report-to-government

I suspect that part of DECC's justification for the short consultation period is that stakeholders have already had an input through this working group. I would not agree with that argument (were it to be raised). The working group members came from a variety of organisations (they are listed in Annex A of the report) but it is still important for property owners and occupiers to be allowed their own say on the MEES proposals – and a six-week period across the summer is not long enough.

My comments on the MEES proposals relating to non-domestic properties

I will use as headings the questions that DECC asks in the consultation paper. I am not mentioning any issues that I believe to be sufficiently covered in the consultation paper.

1. Do you agree with the proposed scope of buildings and leases that should be covered by the minimum standard regulations? If not, what building or lease types should be included or excluded?

The Government acknowledges that there is not yet any Green Deal finance for non-domestic properties (para 30). One wonders what the fall-back position will be if none is in place by April 2018.

It is stated in para 43 that the scope of buildings within MEES will be those within the EPC requirements. This will cause difficulties for listed buildings as no-one knows whether they require EPCs or not.

Even where MEES apparently applies, it will not be relevant to a property where there is no EPC in place (since section 49(1) Energy Act 2011 states that MEES applies only where a property has an EPC). For the proposed "backstop" in 2023, we can expect many properties that would be caught by it not to have EPCs, as many leases will have been granted before EPCs became compulsory in 2007 or thereabouts. But if a landlord deliberately does not obtain an EPC when granting a lease after April 2018, MEES will also not apply, and the landlord's only offence is not to have obtained an EPC, for which the penalty is relatively low. The working group identified this loophole. We do not know if DECC is doing anything to resolve it.

The Government suggests in para 45 excluding very short leases (six months or less) and very long leases (99 years or more).

Further lettings that could be put forward for exclusion are listed in Annex C of the working group's report. They include the following four categories:

(a) where the landlord has no choice over granting the lease

(b) where the transaction is short-term only

(c) where the transaction is more akin to a sale than a letting, although it is being accomplished through the grant of a lease for reasons connected with landlord and tenant law

(d) sub-lettings of parts of buildings.

Categories (b) and (c) have been raised by DECC already.

Under category (a) the working group identified

- Existing contractual arrangements as at April 2018
- Lease granted to a guarantor following insolvency of the tenant
- Lease granted under section 19 Landlord and Tenant (Covenants) Act 1995
- Lease granted by order of the court
- Lease granted by operation of law
- Lease renewal under Landlord and Tenant Act 1954 (see question 8 below)
- Renewal of periodic tenancy
- Extension of lease (effectively an example of a lease granted by operation of law)

Under category (d), I have a major concern. A tenant of part of a building may wish to grant an underlease and MEES will apply to the transaction. But the tenant will not have control of the parts of the building that will enable him to comply with MEES – nor would the landlord want the tenant to try to upgrade the structure of a building, or its plant. This important issue is mentioned in the consultation document (para 47) but only in terms of "consent". I am not convinced that this is sufficient. It is not correct that a tenant of part would need the landlord's "consent" to upgrade the building's air conditioning system. The correct analysis is that the tenant has no right to do so at all. So would this be covered by the "consent" protection? Or should it be dealt with in a more logical fashion?

2. Do you agree that where a property falls below an E EPC rating, the landlord would only be required to make those improvements which could be made at no net or upfront cost, for example through a Green Deal finance arrangement? For those properties that do not meet an E EPC rating, do you have any suggestions for how the process could be streamlined?

This proposal sets out what the Government has always said would be the case.

There is a suggestion in para 58 that the landlord would need to obtain three Green Deal quotes where no measures at all pass the Golden Rule. This seems extreme and suggests that the Government does not have much confidence in the accuracy of Green Deal Assessments. Furthermore, presumably on each occasion the landlord would have to pay for this, which seems unfair.

3. Should the Government allow landlords the option of demonstrating compliance by installing those measures which fall within a maximum payback period, and if so do you have any evidence on an appropriate payback period? Do you have any views on how the process of identifying improvement payback periods should operate?

I cannot see how this differs from the Green Deal Assessment system. The Government seems to be answering its own question in paragraph 62.

4. Do you agree with the proposed method for demonstrating an exemption where works would result in a material net decrease in a property's value? What would be the most appropriate way to set the threshold?

The greatest concern here is the installation of internal wall insulation which could reduce the net lettable area.

I think a simple percentage reduction would be the only safe way to demonstrate a material net decrease in a property's value. The landlord has to know that the exemption has been assessed by an objective method and cannot be challenged later by a Trading Standards Officer.

5. Do you have any evidence that shows the scale of the costs and benefits (including non-financial costs and benefits) associated with improving the energy efficiency of a property, for example time taken to undertake cost effective improvements?

I do not have any comment on this.

6. Does the proposed consents exemption strike the right balance between recognising existing landlord obligations, whilst also ensuring that the allowance is not used as a loophole to avoid undertaking improvements? Do you have any views on how beneficial owner consents should be taken into account?

Paragraphs 76 and 77 raise some difficult issues as to the implications of "unreasonable" conditions attached to consents. I do not understand the second sentence of para 76, which reads "In this case, where the conditions are unreasonable, the landlord would not be expected to proceed." The difficulty is that an "unreasonable" condition has two possible meanings – that it is unreasonable for the person to make it in the first place and that it is unreasonable for the other party to have to comply with it. For example, consider a condition imposed by a supermarket tenant that, in order to fit in with its business requirements, any works can carried out by the landlord only between midnight and 4.00 am. Is that an unreasonable condition, in either of those senses? The regulations need to make this clear.

7. Do you think the regulations should have a phased introduction applying only to new leases to new tenants from 1 April 2018? Do you agree the regulations should also have a backstop, applying to all leases from 1 April 2023? If not, what alternatives do you suggest?

I have always argued for a soft start as it seems unreasonable to require a landlord to revisit an agreement it has already entered into with a tenant (as would be the case with a hard start). Therefore I am pleased to see that the Government favours this option.

However, a backstop has been proposed. This would require all landlords at least to talk to their tenants where leases are already in place now and will run beyond 2023. Presumably the tenant would still be able to refuse consent to the landlord to carry out the works on the basis that the lease does not reserve to the landlord any right to enter the premises for such purposes. Once again we need to ensure that the definition of "consent" is sufficiently wide to cover this possibility.

But even the backstop will not be effective where there is no EPC in place for the building. There is no requirement in the Energy Act 2011 for landlords to obtain an EPC where one does not already exist. So in such a case a landlord might benefit from not obtaining an EPC at that stage. That is counter-intuitive but apparently is the effect of the legislation.

The date for the backstop is a political decision.

8. Should the regulations apply upon lease renewals or extensions where a valid EPC exists for the property?

DECC and I clearly are thinking differently in this area.

DECC believes it is best for the landlord to request permission from the tenant to carry out the works, and for the tenant to refuse if it does not want disruption to its business (or for any other

reason). That would constitute an exemption for the landlord (subject to the "unreasonable conditions" point mentioned above).

I feel that this is against the spirit of MEES. The spirit is that the landlord does not have to upgrade an inefficient building, but if it wishes to let it then it must bring it up to an E rating. The alternative is an empty building (or the landlord can occupy it itself). But in a lease renewal (within the 1954 Act at least) the landlord has no choice about granting a new lease, and therefore should not be required to comply with MEES at all. Even where the lease does not have the protection of the 1954 Act, it is still economically sensible for the parties to renew the lease if they both wish to.

So my view is that lease renewals should not be within MEES at all.

Incidentally, as the consultation paper says, no EPC is required for a lease renewal and so this would only apply where an EPC was already in place. (Actually I do not agree that no EPC is required for a lease renewal – there is no exemption in the underlying EU Directive – but I lost that argument long ago.)

DECC insists on talking about "lease renewals or extensions" refusing to accept that there is no such animal as a "lease extension". It can only take effect as the grant of a new lease.

9. Do you agree that an exemption for properties below an E rating should last for five years, or where the exemption was due to a tenant's refusal to consent, when that tenant leaves, if before five years?

Politically this makes sense.

10. Do you agree that the Government should set a trajectory of standards beyond 2018, and if so, how and when should this be done?

Personally, I consider that it will be difficult enough to enforce a policy that requires a minimum of an E rating. To announce in a few years' time that landlords must repeat the process so that they now need to have (say) a D rating would not be well received.

So if there is an intention to improve the energy efficiency of buildings over time, it would be best to make this clear at the outset. Otherwise there could be a great deal of ill-feeling later.

11. Do you consider where a property has a valid exemption for letting below an E EPC rating that certification of compliance would be helpful? If so should this be voluntary or mandatory? Do you have any other comments regarding compliance and how Trading Standard Officers (TSOs) could be supported with enforcement, for example identifying landlords?

The concept of a certificate of compliance is something that was not considered by the working group and so it is a new issue to me.

There are no sanctions on a tenant who takes a lease of a property that is not compliant with MEES and it seems to me that the types of tenant that are likely to occupy F and G rated properties are (in the main) not likely to be interested in whether or not the landlord has complied with MEES.

So the only people interested in a certificate of compliance would be the landlord and the TSO.

A landlord intent on ignoring MEES would not apply for a voluntary certificate in the first place.

So for a certificate to have any use, it would have to be mandatory. But this would require enormous TSO resource.

Who would pay the cost? It would be inappropriate to require landlords to pay for a compliance certificate when the entire basis of MEES is that there is no upfront cost to the landlord. It would be particularly egregious to charge the landlord for a certificate to say that he is exempt from complying with MEES.

And if a mandatory certification process was put in place, there would need to be an appeal process to cover those occasions when a landlord believed he was exempt but the TSO refused to grant an exemption certificate.

All in all, my current view is that the concept of a mandatory certificate of compliance is unlikely to be practicable.

12. Do you agree that the penalty for non-compliance should be linked to a percentage of a property's rateable value? If so, what percentage should this be? If not, what alternatives do you suggest? Should the Government set a minimum and maximum fine level, and if so at what levels should these be set?

The decisions as to the size of penalty is a political one.

As this is only a civil offence, landlords are likely to compare very carefully the size of any possible penalty with the costs of complying with MEES. This will particularly be the case if there is a maximum penalty.

Landlords are also likely to take into account the fact that there have been very few publicised sanctions under the EPC regulations, and conclude that this is likely to be the same with MEES.

13. Do you consider that the First-tier Tribunal is the appropriate body to hear and determine appeals about decisions regarding non-compliance with the minimum standard regulations? Do you consider that the General Regulatory Chamber Rules of the First-tier Tribunal will suit the handling of these appeals? If not, what tribunal could be used?

This is outside my area of expertise.

14. Do you have any comments not raised under any of the above questions?

We have been told that the changes in building regulations mean that EPC ratings become more strict over time – so that a building with an E rating today might have only an F rating in a few years' time.

We are concerned that this could put a landlord in breach of MEPS. Were a re-rating to happen in, say, 2021, the landlord could grant a lease today (2014) when the building had an E rating. However by the time of the backstop in 2023, the building might be treated as having only an F rating and therefore the landlord would have to take some action under MEES.

15. Do you have any comments or evidence regarding the consultation impact assessment that could inform the final impact assessment, for example the average length of void periods or length of tenant stay in different sectors?

I have not yet read the impact assessment document.