ACS Submission: Non-Domestic Private Rented Sector Minimum Energy Efficiency Standards

ACS (the Association of Convenience Stores) welcomes the opportunity to submit evidence to BEIS' consultation on minimum energy efficiency standards (MEES) for the non-domestic private rented sector. ACS represents 33,500 local shops and petrol forecourts including Co-op, McColls, BP and thousands of independent retailers, many of which trade under brands such as Spar, Nisa and Costcutter.

Two-thirds (69%) convenience stores operated by multiple retailers are rented and 42% of independent convenience stores are rented. Based on sample data from 58 stores we estimate that 50% of convenience retailers will require investment to reach EPC C by 2027[1]. Convenience retailers' investments focus on increasing energy efficiency, for example refrigeration 42% of stores invested in new refrigeration, in-store lighting (30%) and air conditioning (12%)[2] units over the past year. Progress under the MEES supports these objectives – cheaper buildings for retailers to run and a reduced carbon footprint.

Convenience retailers managing multiple properties are beginning to plan refurbishment cycles to meet the expected more stringent EPC B rating by 2030. Small business operators in the sector will require strong landlord relationships, detailed guidance and financial incentives to invest appropriately in the energy efficiency measures required to meet enhanced EPC targets. MEES requires investment in energy efficiency but should also raise awareness of the relevance of buildings to the environmental agenda.

ACS' key recommendations are as follows:

- Boost investment incentives for businesses to ensure energy performance improvements are financially attainable for retailers as MEES standards increase.

- Extend enhanced capital allowances and the 'super deduction' policy beyond 2023 to reflect the proposed MEES timetable.

- Produce detailed guidance alongside a flexible standardised calculator to inform retailers clearly about the measures that can be taken to deliver incremental improvements to energy performance. This should be published well in advance of the first compliance window.

- Proceed with time-limited EPC exemptions for shell and core let properties to allow ratings to reflect actual property usage and minimise the use of pre-tenancy agreements.

- Retain legal responsibility for MEES compliance with landlords but introduce a new 'duty to cooperate' between landlords and tenants.

- Require all convenience stores marketed for let or sale to display up-to-date EPC certificates

For more information on this submission, please contact Steve Dowling, ACS Public Affairs Manager, via steve.dowling@acs.org.uk

[1] ACS – Based on MHCLG Energy Performance of Buildings Data. Accessed May 2021.

[2] ACS Local Shop Report 2020

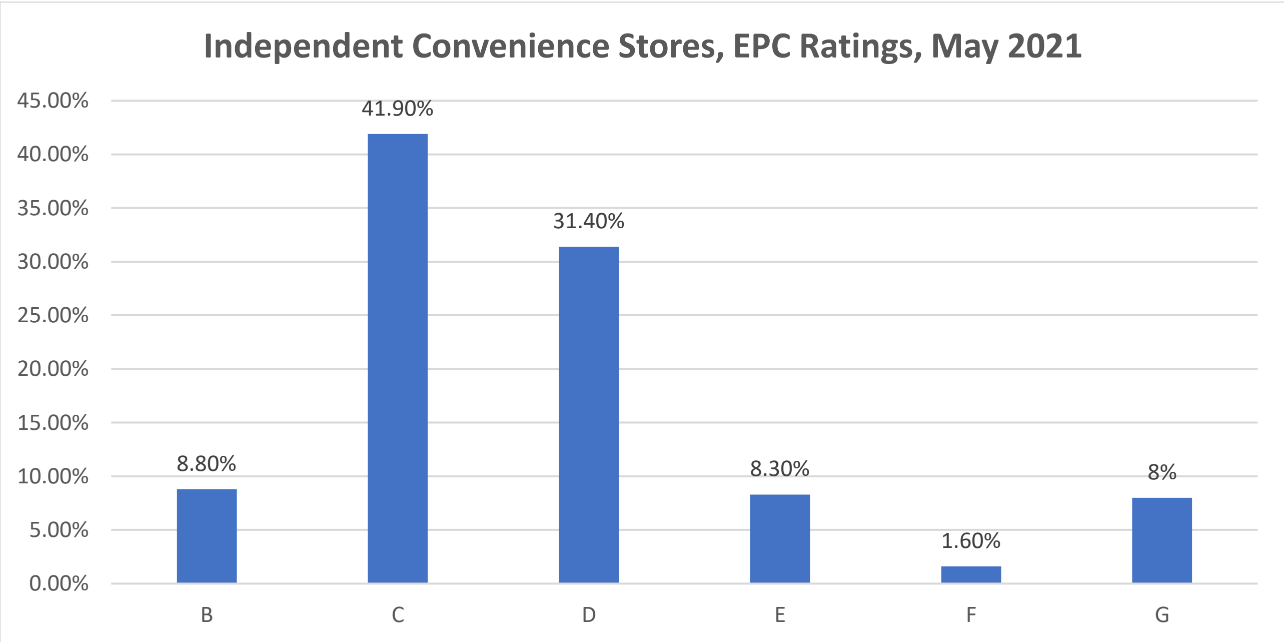
<u>Implementation & Enforcement Framework</u>

Q2) Do you support the Government's proposal to introduce an EPC C interim milestone in 2027?

Yes. An interim milestone will prevent landlords from delaying energy performance improvements until the end of the decade and minimise risks of the EPC timetable causing a single concentrated surge in demand for services related to installing improvements. The earlier energy performance investments an interim milestone would require will also deliver greater carbon savings.

We understand that smaller non-domestic premises can form part of a long tail of less energy efficient properties. One-in-five (20%) independent convenience stores have an EPC rating of E or below, while one-in-three (31%) have an EPC D rating[3].

The graph below presents data gathered from the MHCLG Energy Performance of Buildings Data using a weighted sample according to store size of xx independent convenience stores. These figures exclude stores not constructed, sold or let since 2008 which are not required to have an EPC until 2023. We would expect these stores to have lower energy performance than properties which have required an EPC for sale or letting purposes.



Improving the energy performance of convenience stores below EPC C will require significant capital outlay for most retailers. This outlay is particularly evident within older properties. The prevailing economic impacts of the pandemic on trade and operating costs may also create affordability issues for some tenants unable to afford rent or service charge increases resulting from landlord investments to improve EPC ratings. This is not reflected by the existing payback test or standardised calculator proposal (see Q13). The MEES timetable to 2030 is rightly ambitious but government policy must account for impacts on the wider commercial property market and affordability.

These dynamics require BEIS to review how to improve energy investment incentives alongside the proposed timetable for EPC requirements and enforcement. This should consider enhanced capital

[3] ACS – Based on MHCLG Energy Performance of Buildings Data. Accessed May 2021.

allowances[4] and the energy technology product list[5] which sets out eligibility. We would support the 'super-deduction' capital allowance policy set out at Budget 2021 for plant and machinery to be extended beyond 2023 to reflect the proposed MEES timetable.

A significant proportion of the xx% of owner-occupied convenience stores have not been subject to recent transactions are therefore are not required to have a published EPC. We understand owner-occupied proposals are under development and would welcome informing this consultation process.

Q3) Do you support the Government's proposal to improve the implementation and enforcement of non-domestic MEES by introducing compliance windows?

We support a move towards compliance windows. This will both support business planning and move away from compliance at the point of let, which in practice provides minimal time to make improvements during the property transaction process. Convenience retailers with multiple properties to manage are beginning to plan energy performance improvements according to the proposed timetable for the private non-domestic rented sector.

The enforcement of non-domestic MEES should be applied consistently by local authorities. This requires a set of national enforcement standards to improve certainty and reduce ambiguity on procedures for both businesses and local authorities. We are aware of ongoing work to develop an advisory best practice toolkit on monitoring, compliance and enforcement of the MEES for domestic properties. A similar toolkit would usefully guide non-domestic enforcement. A central database for EPCs with access for councils could also support consistent approaches and a move away from ad-hoc enforcement.

Q4) Do you support the introduction of a six-month exemption for shell and core let properties?

A time-limited exemption is required for shell and core let properties. Convenience retailers typically let unfurnished properties, installing lighting, heating, ventilation and air conditioning as suits the business model, then taking out furnishings when a lease expires and is not renewed. These fitouts significantly impact EPC ratings but are not accounted for under the current regime.

A property let in a shell and core condition is unlikely to meet existing MEES requirements, let alone future enhanced requirements. This can require landlords to install fixtures and fittings that the tenant will immediately remove or the use of pre-tenancy agreements. Pre-tenancy agreements allow a retailer to fitout a store and pay associated costs before legally becoming the tenant. These agreements increase risk for tenants despite not being legally liable for EPC ratings and are not an ideal solution.

An exemption period would allow EPC ratings to reflect the actual use of convenience retail properties, by conducting ratings after fitouts have been completed, without transferring MEES-related responsibilities onto tenants via pre-tenancy agreements.

[4] https://www.gov.uk/capital-allowances/first-year-allowances

[5] https://www.gov.uk/government/publications/enhanced-capital-allowance-scheme-energy-technology-product-list

<u>Supporting Amendments to Deliver the New Framework</u>

Q6) Do you agree with the proposals to amend EPC requirements to support non-domestic MEES under the PRS Regulations?

Strengthening the Energy Performance of Buildings Regulations 2012 to ensure all convenience stores marketed for let or sale have an up-to-date EPC would support property decisions by prospective buyers or tenants.

Requiring an updated EPC at lease renewals should not affect most convenience retailers during the 2020's if the compliance window approach is taken forward. Convenience stores are operated on long leases, typically 10 – 15 years. We support issuing new certificates in these timeframes to support lease negotiations. Updated EPCs should not be required at lease renewal where an updated EPC has already recently been acquired following property improvements or the 2027 or 2030 milestones.

Q13) Do you support the introduction of a standardised calculator to simplify the requirements for the payback test?

The standardised calculator method should be introduced with the three quotes method retained as a backstop for circumstances where exceptional supply chain pressures affect the cost of works. The calculator would prove particularly useful for retailers trading from isolated locations where obtaining three quotes can be more difficult, while a backstop could become more relevant as EPC C and B deadlines approach.

A standardised calculator test must demonstrate the costs and benefits of incremental energy performance improvements as well as 'packages' of improvements to be undertaken simultaneously. This is important to ensure that where the costs are prohibitive to reach a higher EPC rating (e.g. B) from a lower base (e.g. E), energy efficiency improvements are still made to reach a lower but improved rating (e.g. EPC C).

The calculator must be accompanied with effective guidance published well in advance of EPC milestones to support business planning. BEIS resources should detail how to achieve incremental and affordable energy performance improvements, especially as the investments required become more complex to reach higher EPC ratings. Retailers report that existing recommendations that are provided alongside EPC reports vary depending on the strength of the consultant. Some landlords and tenants will want to front-load their investments to reach EPC B, others will be limited and adopt a staged approach in line with the timetable and refurbishment cycles.

Q15) Should the Government seek primary powers to introduce tenant responsibilities duties for MEES compliance under the PRS Regulations for nondomestic properties, and to introduce duties of mutual cooperation for landlord and tenant?

Landlords should retain legal responsibility for MEES compliance, but we would support a new 'duty to cooperate' between landlords and tenants. A duty to cooperate already exists for developing Local Plans in the planning system, introduced by the Localism Act and set out in section 33A of the Planning and Compulsory Purchase Act 2004[6]. A similar approach could place responsibilities on both landlord and tenant to encourage positive, continual partnership on set issues, including energy efficiency improvements. A mediation process could be conducted where this duty to cooperate is not met by either party.

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[6] https://www.legislation.gov.uk/ukpga/2004/5/section/33A

Placing legal responsibility for MEES compliance on landlords has meant less flexibility for retail tenants as the landlord pursues its key related objective to minimise risk. For example, typically tenants are unable to make alterations which could lower the EPC rating, cannot apply for a new EPC without the landlord's consent and must grant property access to landlords to complete works in relation to MEES. We have also seen the growth of pre-tenancy agreements (see Q4).

There is also a potential issue of conflict related to meeting the cost of energy efficiency improvements between landlords and tenants. The RICS Commercial Service Charge Standard states that the costs of obtaining an EPC is not a legitimate service charge cost. However, 'any subsequent costs of improving energy efficiency might comprise a legitimate service charge item, as long as there is a proportionate cost benefit to tenants'[7]. This requires a clear articulation of costs and benefits to tenants and close working relationships based on mutual understanding.

Strengthening landlord-tenant relationships is important to maximising energy efficiency improvements. This has been emphasised by the Covid-19 pandemic. The moratorium on commercial evictions and related measures has created ill feeling between some landlords and tenants. This has created a challenging culture in the medium-term which will take some time and intervention to heal.

The Government needs to produce policy incentives which encourage all landlords and tenants to work together to make energy performance improvements. This should be done via enhanced capital allowances and other green incentives, in order to make the often long-term paybacks of retrofitting worthwhile (see Q2). MHCLG is conducting a separate review of commercial lease legislation which could also affect landlord-tenant dynamics and energy efficiency investments. This review should encourage the regearing of leases to allow for significant retrofitting capital investment, working closely with this BEIS-led review. This will become more important if these ambitious energy efficiency targets begin impacting an already fragile commercial property market.

Supporting the Rollout of Smart Meters

Q16) Do you think that smart meters could play a role in supporting landlords to meet Government energy efficiency requirements such as the non-domestic MEES under the PRS Regulations? What are the key benefits/barriers of smart meters playing a role?

One-in-three (32%) convenience stores have a smart meter installed[8]. Smart meters are valuable for retailers by enabling the tracking of energy usage but there is some caution around the correlation between EPC ratings and actual in-use energy performance as recorded via smart meters. There are many factors which influence power use and carbon emissions, which makes it difficult to show how the installation of x directly results in a measurable reduction in energy usage, when the weather could simply be unusually cold. EPCs must be accurate and trusted to support further energy efficiency investments in line with MEES ambitions.

For more information on this submission, please contact Steve Dowling, ACS Public Affairs Manager, via steve.dowling@acs.org.uk

[7] https://www.rics.org/globalassets/rics-website/media/upholding-professional-standards/sector-standards/real-estate/service-charges-in-commercial-property-1st-edition.pdf

[8] ACS Local Shop Report 2020

Annex A

ABOUT ACS

The Association of Convenience Stores lobbies on behalf of over 46,000 convenience stores across mainland UK on public policy issues that affect their businesses. ACS' membership is comprised of a diverse group of retailers, from small independent family businesses running a single store to large multiple convenience retailers running thousands of stores.

Convenience stores trade in a wide variety of locations, meeting the needs of customers from all backgrounds. These locations range from city centres and high streets, suburban areas such as estates and secondary parades, rural villages and isolated areas, as well as on petrol forecourts and at travel points such as airports and train stations.

ACS | the voice of local shops

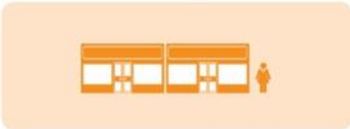
WHO WE REPRESENT

INDEPENDENT RETAILERS

ACS represents over 19,000 independent retailers, polling them quarterly to hear their views and experiences which are used to feed in to Government policy discussions.

These stores are not affiliated to any group, and are often family businesses with low staff and property costs. Independent forecourt operators are included in this category.

SYMBOL GROUPS AND FRANCHISES



ACS represents over 14,000 retailers affiliated with symbol groups. Symbol groups like SPAR, Nisa, Costcutter, Londis, Premier and others provide independent retailers with stock agreements, wholesale deliveries, logistical support and marketing benefits.

Symbol group forecourt operators and franchise providers like One Stop are also included in this category.

MULTIPLE AND CO-OPERATIVE BUSINESSES

ACS represents over 12,000 stores that are owned by multiple and co-operative retailers. These businesses include the Co-Operative, regional co-operative societies, McColls and others.

Unlike symbol group stores, these stores are owned and run centrally by the business. Forecourt multiples and commission operated stores are included in this category.

THE CONVENIENCE SECTOR

In 2018, the total value of sales in the convenience sector was £39.1bn.

The average spend in a typical convenience store transaction is £6.50.

There are 46,262 convenience stores in mainland UK. 72% of stores are operated by independent retailers, either unaffiliated or as part of a symbol group.

The convenience sector provides flexible employment for around 365,000 people.

24% of independent/symbol stores employ family members only.

24% of shop owners work more than 70 hours per week, while 19% take no holiday throughout the year.

70% of business owners are first time investors in the sector.

Convenience stores and Post Offices poll as the two services that have the most positive impact on their local area according to consumers and local councillors.

81% of independent/symbol retailers have engaged in some form of community activity over the last year.

Between August 2017 and May 2018, the convenience sector invested over £814m in stores.

The most popular form of investment in stores is refrigeration.

OUR RESEARCH

ACS polls the views and experiences of the convenience sector regularly to provide up-to-date, robust information on the pressures being faced by retailers of all sizes and ownership types. Our research includes the following regular surveys:

ACS VOICE OF LOCAL SHOPS SURVEY

Regular quarterly survey of over 1,200 retailers, split evenly between independent retailers, symbol group retailers and forecourt retailers. The survey consists of tracker questions and a number of questions that differ each time to help inform ACS' policy work.

ACS INVESTMENT TRACKER

Regular quarterly survey of over 1,200 independent and symbol retailers which is combined with responses from multiple businesses representing over 3,000 stores.

ACS LOCAL SHOP REPORT

Annual survey of over 2,400 independent, symbol and forecourt retailers combined with responses from multiple businesses representing 7,669 stores. The Local Shop Report also draws on data from HIM, IGD, Nielsen and William Reed.

BESPOKE POLLING ON POLICY ISSUES

ACS conducts bespoke polling of its members on a range of policy issues, from crime and responsible retailing to low pay and taxation. This polling is conducted with retailers from all areas of the convenience sector.

For more information and data sources, visit www.acs.org.uk