Heat

Heat Network Investment Project (HNIP) consultation response

London Councils represents London's 32 borough councils and the City of London. It is a cross-party organisation that works on behalf of all of its member authorities regardless of political persuasion.

A. Who should be eligible to apply directly for the capital funding? (Questions 1-4)

London Councils agrees with the premise that the pilot phase of this project should be aimed at Local Authorities. Local authorities have a critically important role in setting the strategic context for, and initiating the development of, district heating networks, due to their local knowledge, capacity for organisation, and key functions as planning authorities and service providers.

London Councils agrees that local authorities, the wider public sector, not-for-profit groups and community groups should be able to apply for capital funding in the full scheme. In theory, by building up the capacity in LAs they will be able to engage with the private sector more effectively, which in turn would help to drive up standards and efficiency of district heating construction projects, in this fledgling sector.

B. What should the Heat Networks Investment Project provide capital funding for? (Questions 5-8)

We believe that the Heat Networks Investment Project should provide funding for commercialisation work where costs are capitalised.

We believe that the HNIP should provide funding for refurbishment of heating and hot water systems inside existing end user premises (including distribution in multi-tenanted properties) that are connected to a new or refurbished heat network supported by HNIP. This is because the pilot needs to prove that district heat networks can be integrated into already existing infrastructure. It would provide learning and experience of this refurbishment work, which could be used to bring costs down in the future, whilst also providing support against any concerns held by the public over the feasibility of district heating as an option.

C. Through which funding mechanisms should the capital funding being deployed? (Questions 9-21)

The funding mechanism deployed (grants, soft loans, central government equity stakes, guarantees) on any given project should be decided in discussion with the relevant local authorities. Therefore a degree of flexibility should be retained when it comes to which mechanism to use on different projects. Different LAs will have different priorities and different economic contexts, and maintaining a suite of options would ensure that a wide section of LAs could participate.

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The biggest barriers to implementation of LA led district heat networks are often cited as obtaining money for feasibility/viability work, and paying up front capital costs when it comes to implementation[1]. Grant funding would provide the easiest way for this challenge to be overcome in the pilot scheme. Capital funding for construction, remuneration, compensation and insurance costs takes away a great deal of uncertainty from developers.

Providing discounted loans (like in Scotland and Sweden) could reduce costs. Government is likely to be able to borrow more cheaply than investors. If it can pass the low interest rates on to investors, this has the potential to reduce overall costs to society. This type of subsidy could also be useful in a world where credit constraints are preventing investors from delivering district heat schemes with good returns[2].

Where grants and soft loans provide obvious benefits to LAs where lack of capital is often a problem, government guarantees could also play a big role, given the burgeoning state of the district heat sector meaning there is still a degree of uncertainty in investment. The Association for Decentralised Energy (ADE) recently published a report that advocated central Government providing a guarantee of future connection capacity to heat networks, which would reduce the risk for investors[3]. This would fall in line with the regulatory frameworks in place for all other utility network investment in the UK[4]. A guarantee linked to the amount of heat demand to be connected and the capital cost of investment would provide the necessary certainty to attract lower cost capital. According to DECC figures there is a £2bn district heating investment opportunity in the UK[5], and this proposal is seen as a way of stimulating this.

D. What decision-making criteria should be used to assess the capital funding applications? (Questions 22-26)

Criteria
While we support that carbon savings is marked as an assumed minimum criteria of any project, more detail should be given, such as a baseline of a certain amount of carbon emissions saved as opposed to traditional heating systems. This could be taken further with projects with innovative solutions to cut carbon emissions further than the assumed minimum criteria amount, contributing favourably to the scoring criteria.

It would seem that the technically future proofed criteria should also be an assumed minimum, to ensure that the lifetime of any project is not impacted negatively by future developments in technology.

Additionality
London Councils agrees with the assertion that the Government should not provide funding to projects that are uneconomic and unlikely to proceed or cause customer detriment, nor projects that are commercially investible (i.e. fully financed by the private sector) and likely to have proceeded without any Government intervention.

London Councils broadly agrees with the high level assessment methodology proposed in Table 3 of the consultation.

E. Monitoring (Questions 27-31)

Measuring and reporting (annually) on the environmental performance of heat networks is crucial – if one of the main aims of pursuing district heating is to deliver carbon savings, then all projects should include some form of carbon offsetting plan, similar to the ones seen in the zero carbon home standard, which the Mayor of London has announced he aims to keep. It is also key that strategic consideration is given to the source of heat, and the impacts on the wider heat and electricity infrastructure. A district heating network covering 250,000 houses could

[1] BRE, CSE, DECC & University of Edinburgh (2013) Research into barriers to deployment of district heating networks.

[2] The CCC & Frontier Economics (2015) Research on district heating and local approaches to heat decarbonisation, Annex 1. Overcoming barriers to district heating.

[3] The ADE (2016) levelling the playing field report: Unlocking heat infrastructure investment

[4] Ofgem (2010) Handbook for implementing the RIIO model, page 100

[5] DECC (2015) Investing in the UK's heat infrastructure: Heat Networks

save between 0.25 and 1.25 Mt CO2 (depending on fuel source) a year compared to conventional heating systems[6].

Additional Comments

Although the role of the Heat Network Delivery Unit (HNDU) isn't being considered specifically in this consultation, London Councils believes that in the interest of improving the development of district heat networks, the role of the HNDU should be extended to support planning and delivery. Due to the uncertainties outlined above, exploring the opportunity for district heating projects is a high risk activity. As stated by the ADE by part funding district heating feasibility studies, HNDU revealed a latent interest in projects from Local Authorities across England and Wales. The Unit's role should be continued and extended to support development all the way from securing planning agreement through to commercialisation and final investment. The excellent work that the Unit has conducted so far, on a relatively small amount of funding from Government (£9.7m) has helped some 200 projects to be explored. Extending the remit of the unit could help this sector mature further.

Given the importance of the issue, London Councils feels it is important that air quality impacts are considered within the HNIP. Domestic boilers account for around 13% of NOx (nitrogen oxides) emissions in London, and therefore the move towards more district heating networks, and the reduction in individual boilers in homes could play a key part in London's strategy to reduce air quality, and something that should be considered.

[6] Poyry, 2009, The potential and costs of DH networks)