## Plot Your Path to Net Zero

# A Focus on Funding for the Public Sector

#RoadToNetZero

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# What's inside...

# Introduction

**The UK is now on a 30-year journey to hit net zero carbon emissions by 2050. The changes required are huge in terms of the way our buildings will be heated, the cars we will drive and generally how both organisations and the energy grid will operate. And, these changes will need to start now if we have any chance of achieving our target.**

With the pressure on to lead the way and become both exemplars and facilitators on the path to net zero, decarbonisation commitments from the public sector will be absolutely crucial to reaching our 2050 target, and many organisations have already set ambitious goals for reducing carbon emissions across their operations.

However, this does not come without its challenges. When we are working with public sector organisations on their decarbonisation strategies, two of the most common questions we are asked are, 'how much will this cost?' and 'where can we find funding?'.

The Public Sector Decarbonisation Scheme (PSDS) was set up to help some organisations answer those questions. Now in its second phase, with applications for the 2021-22 financial year having closed after less than one week in April, grants awarded by the scheme this time were focused on helping with heat decarbonisation. Competition for a slice of the £75 million grant fund was fierce, and while Phase 3 will be worth watching out for, grants will have a cap (set at £5 million during Phase 2) and won't be available to everyone.

For most organisations, decarbonisation projects are self-funded, but capital expenditure (CAPEX) is particularly tough to find during this period of major recovery. Making the case for investment in energy efficiency and larger decarbonisation measures can therefore be challenging. In our previous report - 'Plot Your Path to Net Zero: A Focus on Sustainable On-Site Generation' - one of the primary barriers to investment was securing funding.

Added to this, at the time of writing, we are still awaiting guidance from HM Treasury on how the UK's net zero ambition will be funded. In its forthcoming Net Zero Review, we are expecting details of the contribution organisations of all types will be expected to make. Last year, our 'Your Business Blueprint - The Road to Net Zero' report revealed concerns from organisations about the potential economic impact on their business of funding the transition. There was also a difference in opinion as to who should fund the majority of the transition - when asked to rank who should bear the cost, respondents were split between the government and large energy intensive industries, with financial institutions also ranking highly.

That said, there was an acknowledgement that there would be an obligation on organisations to contribute, so in this report, we have revisited the theme of funding net zero, to see if these views have changed following the publication of the Energy White Paper in December 2020 and the Industrial Decarbonisation Strategy in March 2021. We also examine the funding strategies and options available to organisations, as well as provide practical advice for how to make the investment case for low-carbon measures when budgets are tight

We hope you find it useful.

**Sarah Middleton**

Public Sector Manager, I&C Energy Solutions,
E.ON UK and npower Business Solutions (nBS)

# Executive summary

**We consulted with more than 60 organisations across areas including the public sector, manufacturing and transport to find out how they fund sustainability projects, who should bear the most responsibility for funding the net zero transition, and whether they believe the existing government policies go far enough to encourage investment.**

### Organisations use their own finance to fund projects, and recognise the importance of doing so

The majority (67%) of organisations we spoke to use their own funds to finance energy efficiency and sustainability projects, and for many, achieving net zero will require them to invest up to 15% of their annual turnover. That said, despite the potential significant cost, the majority believed that the climate benefits outweighed the cost impact.

### Organisations are concerned about the cost impact of funding net zero

With the government's interim Net Zero Review stating that the transition to net zero will require new investment from organisations and that 'these costs are primarily capital expenditures', 70% of our respondents said they were very or slightly concerned about the potential cost impact.

In terms of who should contribute the majority of the funding for the net zero transition, our respondents believe that large, energy intensive users and the government should foot the bill. A large number of organisations also said that financial institutions will play a key role.

### Current government policy does not go far enough to support businesses

Our findings show that more support and certainty is needed from the government to help organisations make the necessary changes to their operations. When asked whether they felt the most recent government policies and strategies offer enough incentives to invest in decarbonisation measures, 75% of our respondents said no.

Investigating alternative ways to fund capital projects, such as government grants or other finance options, could help to reduce the financial burden of the low-carbon transition and for some, the PSDS could provide welcome financial support; although this has been capped at £5 million per project during Phase 2.

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Section

# Funding net zero: what are organisations doing?

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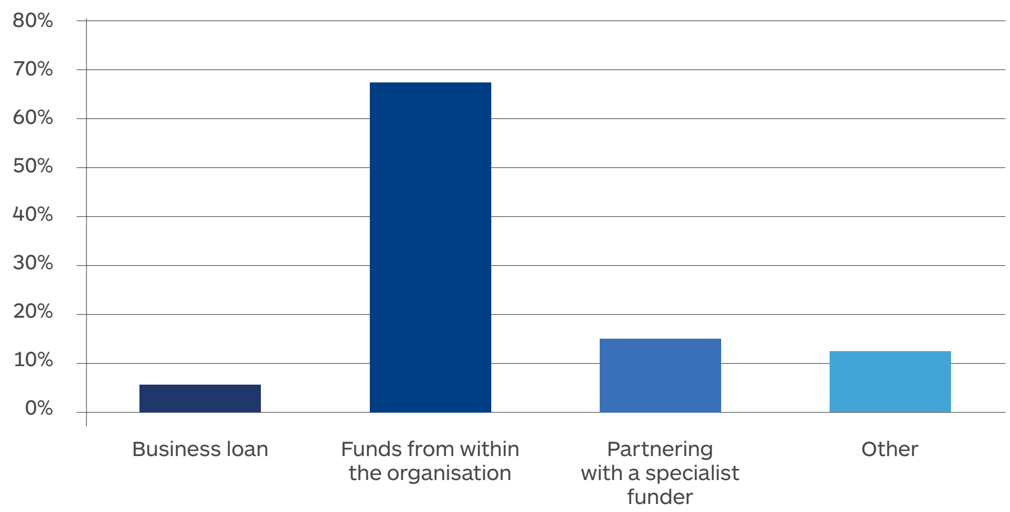
# Funding net zero: what are businesses doing?

When it comes to financing energy efficiency and sustainability projects, the majority (67%) of organisations we spoke to use their own funds, with a smaller number choosing to partner with a specialist funder. (Figure 1.)

Other answers revealed that some organisations had been successful in securing additional funding via grants from external organisations including Innovate UK and the Department for Business, Energy and Industrial Strategy (BEIS). Some respondents said that a combination of grants and loans had allowed them to invest and, interestingly, one respondent was able to secure €2 million in European Commission (EC) grants 'owing to the lack of UK grants' available.

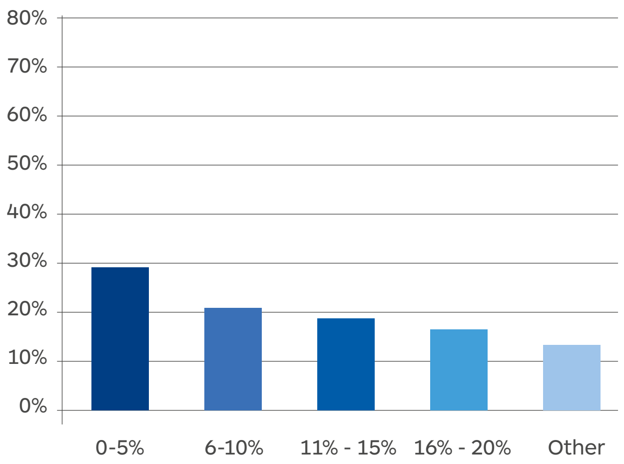
For on-site projects, Power Purchase Agreements (PPAs) were mentioned and some of the respondents from public sector organisations had accessed funding from the PSDS. To be eligible, applicants needed to be using a fossil-fuelled heating system, with the heating system in question coming to the end of its useful life.

**Figure 1: How would your organisation usually fund capital investment energy/sustainability projects?**



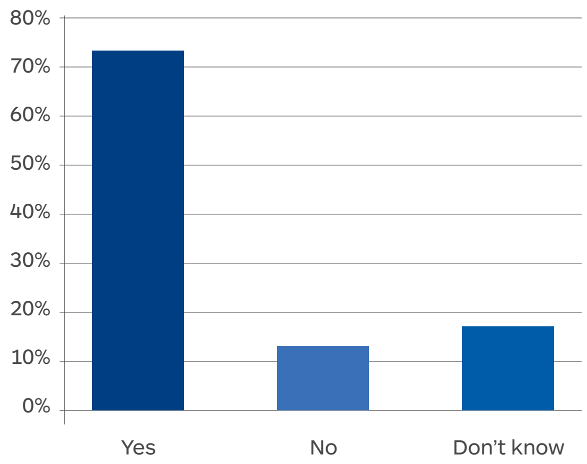
When asked about how much of their annual turnover organisations predicted they would need to allocate to fund their sustainability ambitions, the answers revealed that 70% felt it could be up to 15%, while one in six (16%) believed that this could be as much as 20%. Some anticipated it would cost even more to hit the net zero timelines set out by the government. (Figure 2.)

**Figure 2: How much of your annual turnover do you think you will need to invest to put measures in place to decarbonise your organisation?**




That said, the majority of respondents (72%) were in agreement that the climate benefits of funding their decarbonisation plans outweigh the potential cost impact. (Figure 3.)

**Figure 3: Do you believe the climate benefits of funding net zero outweigh the potential cost impact?**

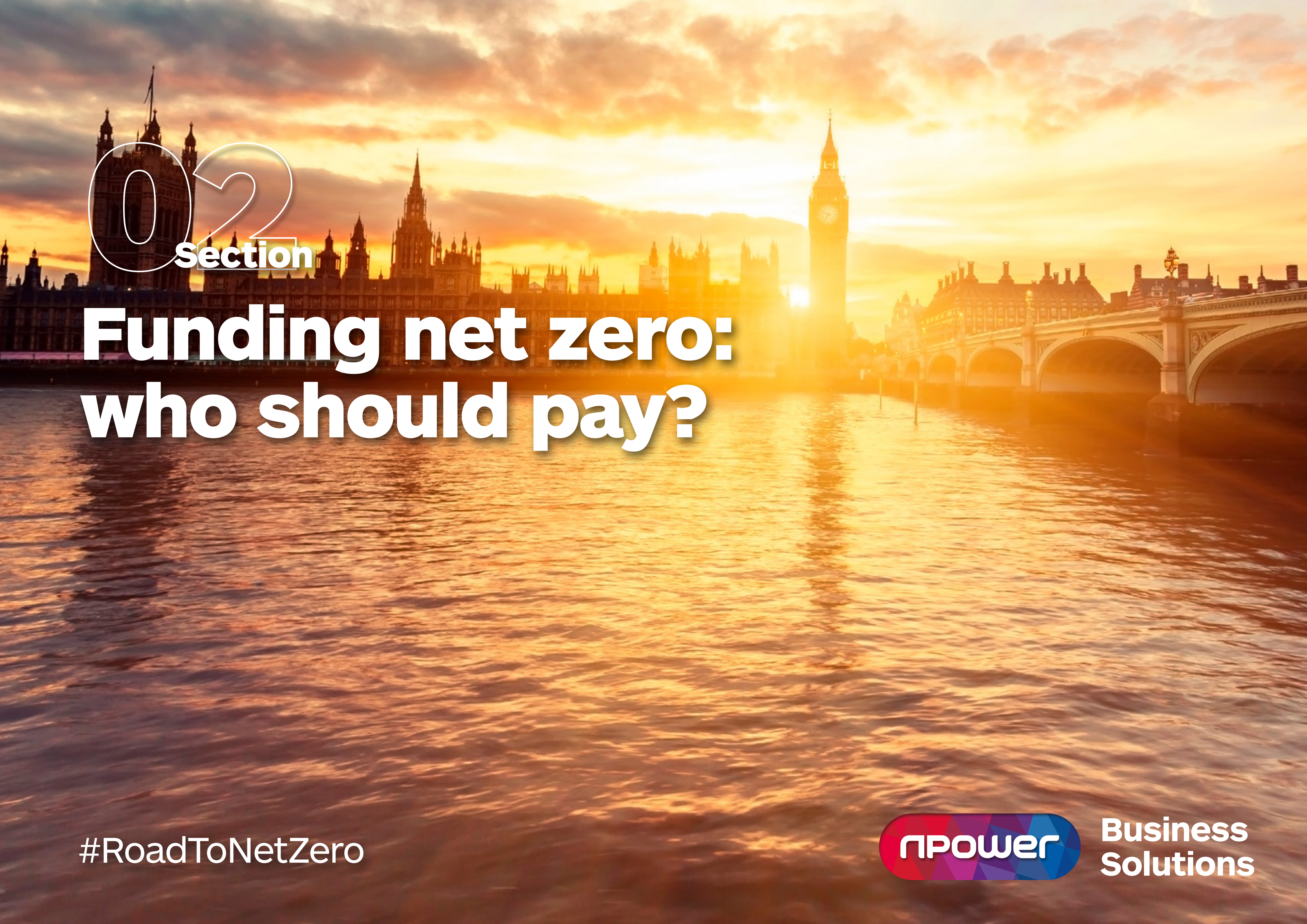



**The government's 2020 Energy White Paper revealed that emissions from homes, commercial premises and public sector buildings account for 19% of total UK greenhouse gas emissions (GHG), making buildings the second largest source of emissions. Public sector buildings account for 9% of emissions from buildings.[1]**

1. https://www.gov.uk/government/publications/energy-white-paper-powering-our-net-zero-future/energy-white-paper-powering-our-net-zero-future-accessible-html-version

Section 02

# Funding net zero: who should pay?



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# Funding net zero: who should pay?

In its interim Net Zero Review, published in December 2020, HM Treasury said that: “Reaching net zero will be a collective effort across households, businesses and the government.” The report contained initial analysis, rather than firm policy recommendations, ahead of the publication of the Review’s final report, which is expected imminently in 2021.

What is clear from the report is that transition to net zero requires new investment and that ‘these costs are primarily capital expenditures, but will also encompass changes to the long-term operating costs of the economy.’

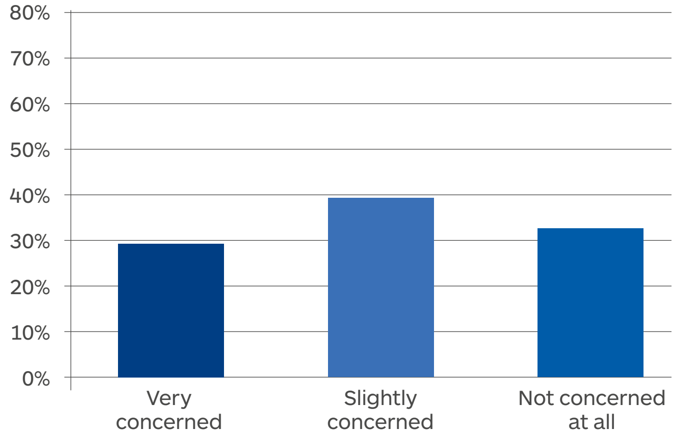
While the scale of the investment will differ depending on the organisation’s size and sector, the report says that ‘the net impact will depend on the business’s current carbon exposure and their ability to change consumption patterns or business processes.’ For example, how organisations make their buildings more efficient will be key, as will replacing petrol or diesel cars with electric vehicles (EVs).

It also said that areas to take into account included the ‘timing of natural investment cycles, the rate at which technology costs fall, innovation and nationwide system-level decisions, such as the choice of energy mix over the next decade.’[2]

As mentioned earlier, in our 2020 report - ‘Your Business Blueprint - The Road to Net Zero’ - 46% of organisations expressed concern about the potential impact of funding the low-carbon transition on their organisation.

In our latest feedback, this has grown, with 40% saying they were slightly concerned, and a further 30% saying they were very concerned. (Figure 4.)

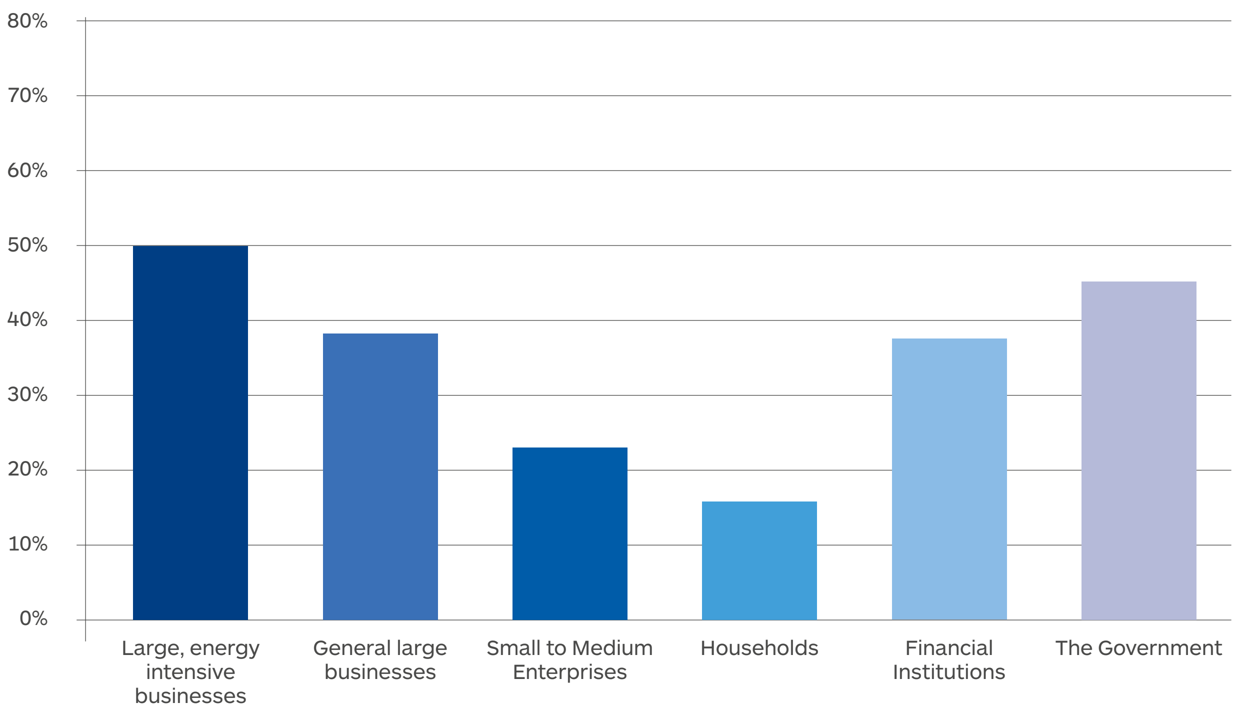
**Figure 4: How concerned are you about the potential additional cost to your organisation to fund the net zero transition?**




2. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/945827/Net_Zero_Review_interim_report.pdf

Opinions on who should contribute the majority of the funding towards the net zero transition haven't changed since we last consulted with organisations, with the vote still split between large, energy intensive businesses and the government. (Figure 5.)

**Figure 5: Which group do you believe should contribute the majority of funding for the net zero transition?**





Interestingly, for this report we also asked a further question about whether financial institutions will play a vital role in supporting organisations by helping to fund the net zero transition. As indicated in 'Figure 6', the overwhelming majority (82%) either strongly agreed or agreed that this was the case.

With this in mind, in the March 2021 Budget, the Chancellor of the Exchequer confirmed a new National Infrastructure Bank - which was recently launched in Leeds - and that its primary focus will be on investment in public and private green projects. The Bank will have an initial £12 billion capitalisation.

We asked our respondents whether they thought this would be enough to spur the necessary investment needed for low-carbon measures. As 'Figure 7' shows, while just over one fifth (22%) thought it would, 44% thought it wouldn't go far enough.

**Figure 6: To what extent do you agree with the following statement: "financial institutions will play a crucial role in funding the net zero transition"?**

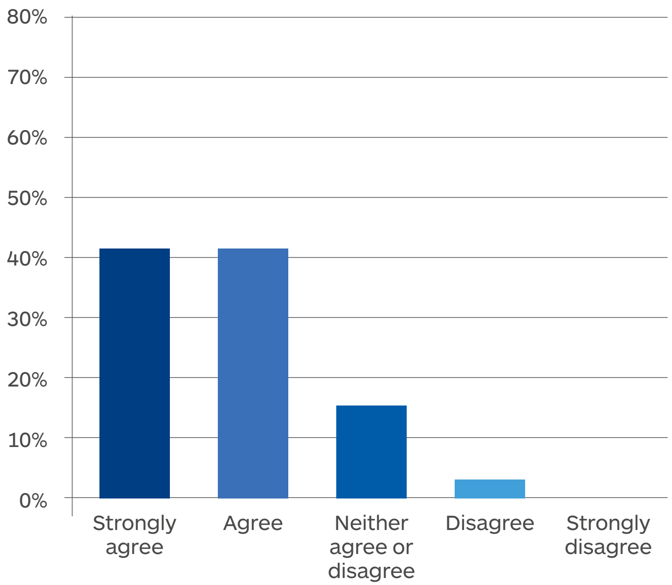
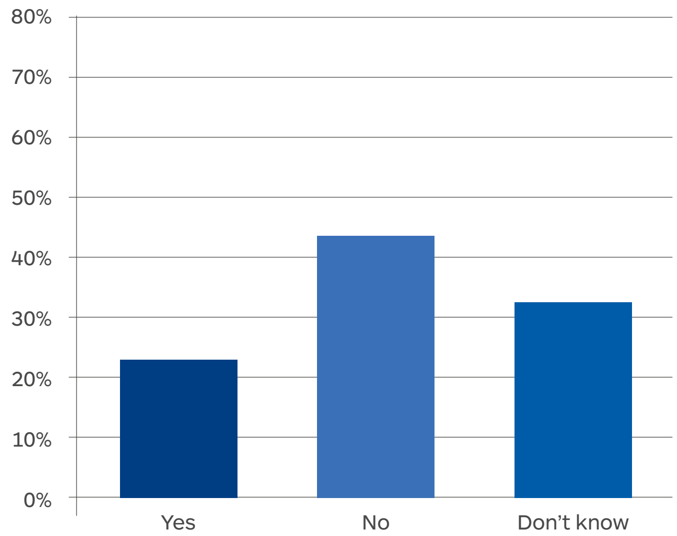



**Figure 7: Do you believe the National Infrastructure Bank's initial £12 billion capitalisation is enough to spur investment from organisations in low-carbon measures?**



Section 03

# Funding net zero: options for public sector organisations

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# Funding net zero: options for public sector organisations

As outlined earlier in this report, the majority of organisations use their own funds to finance energy efficiency and low-carbon projects. As expected, the amount varies depending on the organisations' size and sector, with some anticipating they will need to spend in excess of 15% of their annual turnover to decarbonise their operations.

During a time of economic uncertainty, investigating alternative ways to fund capital projects - such as government grants or other finance options - could provide some welcome relief and reduce the financial burden of the low-carbon transition.

That said, our findings show that more support and certainty is needed from the government to help organisations make the necessary changes to their operations. When asked whether they felt the most recent government policies and strategies - including the Ten Point Plan, Energy White Paper and Industrial Decarbonisation Strategy - offer enough incentives to invest in decarbonisation measures - 75% of our respondents said no.

So, what are the current funding options available to organisations if securing CAPEX is challenging?

### The Public Sector Decarbonisation Scheme (PSDS)

The Industrial Decarbonisation Strategy, published in March 2021, confirmed a second round of funding for decarbonisation projects across England through the PSDS. The aim of this is to reduce carbon emissions from public buildings, and many local authorities, NHS Trusts and other public sector organisations benefited from Phase 1 of the scheme, using funds to install measures to make their properties more efficient.

Phase 2 of this scheme provided £75 million of grant funding. It had a stronger focus on heat decarbonisation than Phase 1, in order to deliver greater carbon emission reductions. Phase 2 opened on 7 April 2021 and closed to applications less than a week later on 13 April 2021. Successful projects need to be completed by 31 March 2022.

There is currently no confirmation that PSDS will award a third phase of funding but this will be worth watching out for later in the year.

Salix Finance Ltd - which is a non-departmental public body, wholly owned by the government - is currently delivering all allocated funding for Phases 1 and 2 of the PSDS.

### Power Purchase Agreements (PPAs)

PPAs are a popular way of financing on-site generation projects, such as solar photovoltaic (PV) or wind, when securing up front capital is an issue. They are a long-term agreement where a third party funder installs and manages the on-site asset and the organisation then buys the energy from the funder over the course of a long-term supply contract, negating the need for up front investment.

If suitability for on-site generation at a particular site is also an issue, businesses can still benefit from a PPA to purchase energy from a local renewable energy source.

### Local authority energy efficiency schemes

For non-industrial or less energy intensive organisations, there are other potential options to secure grants for energy efficiency projects. For example, many local authorities operate energy efficiency schemes to help fund measures for smaller organisations - a useful roundup can be found here.

> **"The transition in our energy systems is about decarbonisation, decentralisation and democratisation. The public sector is naturally at the heart of this: it governs our democracy, it is decentralised, and it is setting itself targets for reaching net-zero."**
>
> Joanne Wade, Chief Strategic Advisor,
> The Association for Decentralised Energy (ADE)[3]

### Industrial Energy Transformation Fund

While the government has announced funding to support the development of major new technologies that will help decarbonise industry in the longer term, such as carbon capture, utilisation and storage (CCUS) and low-carbon hydrogen production, there are also existing schemes some businesses may be eligible for now.

In fact, the government says it has £5 billion of funding available to help UK businesses become greener and to support their net zero journeys. These include the Industrial Energy Transformation Fund, which is a £289 million fund to help energy intensive businesses to cut their energy invoices and carbon emissions by investing in energy efficiency and low-carbon technologies.

Eligibility for government schemes will vary depending on the business's size and sector - you can check if your organisation is eligible for the latest schemes here.

### Green Heat Network Fund (GHNF) Transition Scheme

Recently announced by BEIS, the GHNF is a capital grant fund open to public, private, and third sector applicants in England. It will build on the progress made by the Heat Network Investment Project (HNIP), by supporting the development of low and zero carbon heat networks (including the supply of cooling).

The purpose of the transition scheme will be to better ensure that low-carbon heat network projects are construction-ready in time to apply to the GHNF full scheme when it opens for applications in the next financial year (April 2022 - March 2023).

The GHNF Transition Scheme will open to funding applications on 5 July 2021 and offer commercialisation funding only.

### Finding the right option for your organisation

We have outlined just some of the options available to Public Sector organisations. There are also flexible funding models for certain types of projects, just speak to your energy partner about what you would like to achieve and they can help you with a funding option that is right for your organisation.

3. openaccessgovernment.org/energy-public-sector-has-the-power-to-drive-the-net-zero-transition/104014/

Section 04

# The expert view: making the case for net zero investment

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# The expert view: making the case for net zero investment

David Baker, Development Manager, I&C Energy Solutions, E.ON UK and npower Business Solutions (nBS)

As we've examined in this report, organisations overwhelmingly support the role they will need to play in the UK's net zero ambition. However, concerns around releasing capital to fund projects - particularly during times of economic uncertainty - mean that sustainability initiatives could be put on hold if more pressing financial needs are identified.

That said, while 2050 may seem a long way off, significant action needs to be taken now to have the necessary impact so we can achieve our ambitious carbon reduction targets.

So, how can organisations make the investment case for net zero? For us there are four key areas to focus on:

**Small changes can make a big difference**

When it comes to energy efficiency and low-carbon investment, there is often the misconception that it will immediately require major capital expenditure. This is not always the case as 'quick wins' such as switching to more efficient lighting, air conditioning and heating can result in significant energy savings without much upfront cost.

An energy audit will be able to identify where some of the most effective low-cost, relatively small changes can be made to result in maximum savings - savings that can then be redirected into further sustainability measures. Energy efficiency really is a 'no regrets' action and can be implemented relatively quickly.

**Demonstrate return on investment (ROI)**

For larger projects that require greater amounts of funding, such as installing an energy management system or an on-site asset, it is important to demonstrate the short, medium and long-term benefits it will bring to the business. For example, depending on the project, these could include:

- Reduction in carbon emissions
- Reduction in energy invoices
- Improved reputation
- Greater employee engagement
- Higher self-sufficiency i.e. less reliance on the grid
- Opportunity for additional revenue streams, for example via Demand Side Response (DSR)

Having either real-life examples or robust data modelling to show the potential positive impact of a project is key to securing investment.

### Explore additional funding options

As outlined earlier in this report, it is important to do your research as to what additional funding options are available before you commit to a project, as it may be your organisation is eligible for government funding or a local authority grant, particularly if you work in an energy intensive sector.

Similarly, PPAs can help fund on-site generation with minimal financial risk, and there are also flexible funding options available for organisations that may want to switch from a PPA to owning an asset during the PPA's term - just speak to your energy partner to see what the opportunities are for your organisation.

### Showcase results

If you have secured funding for a sustainability project, it is vital to demonstrate the results as this will help unlock further investment for future initiatives.

This is where good data management is crucial to understand how the measures are performing and to enable you to identify improvements. These could include looking at how adapting times of use, the efficiency of infrastructure and processes, and changing employee behaviour can impact the success of a project. It will also help you to demonstrate a clear ROI in terms of reducing emissions and costs.

# How we can help

**However ambitious your sustainability goals are, our business energy experts can help your organisation to make the case for net zero investment.**


## Contact us

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