MAYOR OF LONDON

Allowable Solutions – consultation response

October 2013

Principles of proposed mechanisms

The Mayor of London is in agreement with the principles proposed –

- Affordability for developers and a regime that should not inhibit development
- Creation of market mechanisms to drive cost-effective solutions
- Funding measures that would not otherwise get delivered

However, the principles and benefits of localism have not been given sufficient consideration. The probable impacts of the proposals on London and other cities should give cause to the Government to consider putting geographical boundaries around AS, consider alternatives to a fixed price cap and give further thought to whether some of the energy supply solutions envisaged will actually be supported under the proposed mechanisms.

Likely impacts on London

Under the proposed mechanisms, there is a strong likelihood that London will provide much of the funds for AS but will be out-competed on price. Without revisions, London will again subsidise the rest of the UK as it does with related fiscal burdens such as Stamp Duty and energy supplier obligation programmes. Government ministers will be aware of the recent recommendations of the London Finance Commission with regard to fiscal devolution, which are now also supported by the Core Cities Group.

This is not just an issue of cost-effective carbon emissions savings. There are notable energy system and associated economic advantages of London keeping its AS. The scale of inward investment in retrofit and low carbon heat and power supply in London that AS could stimulate would reduce the pressure on upstream generators and on London's already over-burdened electricity distribution network.

The competitiveness of London as a world city is integral to the UK economy, yet our building stock is inefficient in comparison to competitor cities. Electricity demand growth of between 1-4 per cent/annum is expected as London grows and becomes even more dense. The prospects of energy supply uncertainty and higher energy costs put London at a comparative disadvantage to our international competitors.

London's housing market and rate of built environment development is quite different to the rest of the UK. The value of that development to and its impacts upon the London and UK economy should be recognised. That does not mean that tight onsite carbon reduction requirements should be relaxed. Rather it means that the externalities of the unmitigated carbon emissions and increased energy demand impact should be addressed within London.

Key areas of concern with the proposals

i. London's disproportionate burden under the proposals

The scale of London's potential contribution to Allowable Solutions

The Greater London Authority (GLA), on behalf of the Mayor of London, is the deciding planning authority for all planning applications of "potential strategic importance" in London; that is all developments with over 150 housing units and all applications (housing and otherwise) over 15,000sqm. In 2012, in implementing the London Plan, the Mayor reviewed applications accounting for almost 56,000 housing units, almost all of which were flats.

Since 2010, the London Plan has required all London developments to meet 2010 Building Regulations carbon targets through energy efficiency alone and to deliver a further 25 per cent improvement on Building Regulations in total – equivalent to the Zero Carbon Hub's proposed carbon compliance level for 2016. The GLA obligates all strategic developments to submit a detailed energy assessment, all of which are reviewed against that obligation and against the requirement to consider, in hierarchical order, energy efficiency, heat network connection, combined heat and power and renewables. In 2012, developments were achieving an average of a 30 per cent carbon saving improvement on 2010 Building Regulations, without viability concerns being raised.

London's contribution to national housing targets over the coming years is projected to be between 50-60,000 new homes per annum – one quarter of the total. If it is assumed that these are all flats, with residual carbon emissions of 0.75 tonnes/flat, to be delivered through Allowable Solutions (AS), this could result in London housing development generating up to £82.5m/annum under the proposed regime (assuming the £60/t price cap).

Should Government choose to extend AS to commercial development, the amounts generated in London would be significantly higher. Taking a current example, there is a large mixed-use development currently at Stage 1 of its consideration by the Mayor which, based on its energy statement, could generate between £5m and £10m on its own.

The relative cost of delivering carbon saving measures in London

The consultation's indicative list of measures that could be funded through AS includes many that would be appropriate to London. However, London is less likely to benefit from them than other parts of the country, because London's building stock and the complex logistics of working in London make it more expensive to install both retrofit and energy supply measures.

Homes retrofit provides a key example. Sixty per cent of London's homes have solid walls. Fifty per cent of homes are flats. London has half of all conservation areas and the highest proportion of private rented homes. These factors, combined with logistical difficulties of working in London meant that despite the fact that London has 12 per cent of the UK housing stock, it received only 5 per cent of CERT and CESP funding.

Projects that can combine both ECO funding and AS are likely to prove amongst the most cost-effective routes for AS. Twenty per cent of ECO-eligible households or areas are located in London. However, London is again losing out under ECO as cheaper projects are found elsewhere. There is a strong likelihood then that when ECO and AS projects are bundled

together, this will have the doubling effect of drawing investment through both mechanisms away from London.

The burden put upon London's energy infrastructure by new development

Increased energy use in a local area puts additional burden on the local energy infrastructure. In parts of London, the electricity distribution network is already 'at or above firm capacity'. Large new developments often require investment in new substations. Londoners and London businesses bear this cost. They also bear the burden of increased NO_x emissions from gas use in new developments. It is therefore appropriate that developers should contribute to AS in London that would reduce energy consumption and offset these burdens. This would accord with government's principle that local authorities that host growth should get a local benefit from doing so.

The current proposals are likely to mean that AS in London are uncompetitive. In combination with proposals under the Housing Standards Review, there is significant risk that the well-established plans in London to support the deployment of decentralised energy and heat networks through the planning system will be undermined. Developers may find it easier to comply with building regulations by proposing individual, rather than communal heating systems. Individual gas systems will be harder to retrofit to lower carbon sources in future. Individual heat pumps will add significantly to the burden on an already stressed electricity distribution network. Strategic developments in London are already demonstrating the viability of meeting proposed carbon compliance levels. London must have the means through the planning system and via *local* AS to support the retrofit of buildings and the deployment of energy supply solutions that allow it to have affordable, secure, low carbon energy long-term without jeopardising development viability.

ii. Alternatives appropriate to London and the ambitions of the scheme

Whilst we accept the rationale for the proposed price cap and understand the preference for a national scheme, we are of the view that amendments to the delivery model could enhance the AS contribution to the types of measures envisaged in chapter 4 of the consultation.

The London housing market is increasingly distinct. The table below indicates the burden of AS as a percentage of the average sale price of a new build home in London. Whilst the figures do not account for land values, they do provide an indication that the relative burden on developers will vary markedly from area to area under the price cap proposals. A more appropriate cap would be one that accounted for this variability and the geographical variability in the cost of carbon saving measures. There tends to be a natural correlation between density, land value and the cost of the carbon saving measured envisaged under the AS proposals; each of those values being significantly higher in London than elsewhere. Several London boroughs have undertaken studies that estimate the costs of carbon saving measures that could be funded under similar schemes. All of those estimates are in the higher range.

	Price (£) (at April 2013)	% of sale price at £36/tCO_2	% of sale price at £60/tCO_2	% of sale price at £90/tCO_2
London	415,540	0.20	0.33	**0.50**
Eng + Wales	233,822	0.35	**0.59**	0.88

http://www.thisismoney.co.uk/money/mortgageshome/article-2316479/New-build-prices-rise-12--says-Halifax-London-market-powers-2007-levels-says-Hometrack.html

A cap that is a factor of the value of new development – say 0.5 per cent of new build sale price, for example – along with a regional boundary for AS, could allow regional markets to emerge with an AS price that fluctuates with the housing market and better reflects the actual price of carbon saving measures in the area where the developer is building. Most of the measures that are envisaged to be supported under the AS proposals are most suitable in dense urban environments. These changes would allow London and other cities to become key markets for those solutions supporting the low carbon economy, without constraining development.

iii. Heat networks

It is unlikely that district heating will be funded under AS without revisions to the proposals. The development of decentralised heat and power generation and district heating forms an integral part of London's and other cities' contribution to the delivery of Government's heat strategy. It appears to be an ambition for AS that they should support district heating and it might often make sense for a developer to contribute to a district heating network if his/her future developments could in turn receive low carbon affordable heat from that network. However, except perhaps if the central fund route were the sole option, it is difficult to see how the proposed options would support district heating. The reasons for this are as follows –

- Lead-in times for district heating are long compared to simpler solutions
- The ex-ante carbon saving valuation and verification of projects is more difficult
- The lifetime carbon saving potential of district heating (particularly where lower carbon heat sources can replace higher carbon ones over time) is harder to account for

iv. Persistence factors

The persistence factors (lifetime carbon saving) of AS should be accounted for. This would avoid a 'race to the bottom' and would ensure more complex measures that have greater long-term carbon saving potential are genuinely considered.

v. Ex-ante verification

Methods that enable ex-ante verification of more complex measures should also be considered, allowing them to compete on a more level playing field.

vi. Timeframe for delivery

A suitable timeframe over which AS must be delivered must be set. Five years would seem appropriate.

vii. Menu of options

If the intention is to create a suitable market mechanism, then the brokerage scheme should be the only option for developers. This will have the added benefit of improved transparency. The other options are likely to undermine the brokerage. The 'do it yourself' option is open to corruption, whilst allowing developers to 'bank the difference' on schemes agreed prior to 2016 will create perverse incentives, disrupt the planning system and will not incentivise house building. A national fund would likely out-compete other options, reducing the scheme to a ring-fenced tax to support a few big projects.