HEAT NETWORKS
INVESTMENT PROJECT

HNIP main scheme clarification

Stage 2 Financial Model

Triple Point
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INVESTMENT MANAGEMENT

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Stage 2 Financial Model

WHAT IS THE STAGE 2 FINANCIAL MODEL?

The Stage 2 Financial Model includes all the information (refreshed if relevant) stated in a Stage 1 Financial Model, including pre- and post- HNP intervention cashflows. The Stage 2 Financial Model is expected to be an incremental development of the Stage 1 Financial Model, not a completely new model. The information we expect to see included in the financial models is set out in Appendix E of the Application Guidance[1].

In addition to the information contained within the Stage 1 Financial Model, the Stage 2 Financial Model includes:

- Inflation
- Tax
- Financing costs
- Financing sensitivities
- Financial statements
- Commercial Structure
- Financing ratios (if relevant)
- Databook

WHO SUBMITS A STAGE 2 MODEL?

Applicants who are delivering their projects in-house (i.e. not through an ESCO/SPV but where the project is integrated into the applicant's main business and delivered on balance sheet), will only be required to submit a Stage 1 Financial Model. Applicants who are delivering their projects through a separate company/SPV, and who are applying for Commercialisation and Construction funding, will be required to submit a Stage 1 Financial Model at application stage and to develop a Stage 2 Financial Model during the commercialisation stage, prior to drawing HNIP construction funding. It is anticipated that applicants for Commercialisation and Construction funding may include the cost of developing the Stage 2 Financial Model in their commercialisation budgets.

Applicants who are delivering their projects through a separate company/SPV, and who are applying for Construction funding, will be required to submit a Stage 2 Financial Model at application stage.

Projects delivered through an SPV include those where the applicant is receiving the HNIP funding and on-investing it in to an SPV, and those where the SPV is receiving the HNIP funding directly.

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1 Available online: https://www.gov.uk/government/publications/apply-for-heat-networks-investment-project-hnip-funding

The Financial Model requirements are summarised in the table below:

TYPE OF APPLICATION	IN-HOUSE DELIVERY	DELIVERY THROUGH A SEPARATE COMPANY / SPV
Commercialisation and Construction Funding	Stage 1 Financial Model at application stage	Stage 1 Financial Model at application stage Stage 2 Financial Model prior to construction drawdown
Construction Funding only	Stage 1 Financial Model at application stage	Stage 2 Financial Model at application stage

WHY IS A STAGE 2 FINANCIAL MODEL REQUIRED?

The Stage 2 Financial Model is required in order to show that the applicant has considered the financial implications for the project of, amongst other things, inflation, tax, business rates and financing costs. The Stage 2 Financial Model outputs indicate whether the project is financially viable on a post-inflation, post-tax, post-financing basis. This is important for our assessment of the financial robustness of the project.

By adopting a familiar and consistent approach, the ability for commercial funders to invest in the heat network sector is expected to be increased. This should move the sector closer to the professionalised, self-sustaining state that we aspire to achieve.

We will utilise key outputs of an applicant's financial model to make comparisons with the outputs from the Financial and Economic Assessment Model (FEAM) and if there are significant differences then we may seek clarification from the applicant. If the mismatch cannot be resolved within the assessment window, then the application may be rejected; however, the project can re-apply in a subsequent HNIP funding round.

WHAT INFORMATION IS NEEDED WITHIN THE STAGE 2 FINANCIAL MODEL?

Full details as to what information is required are outlined in Appendix D – Funding Plans and Appendix E – Financial model specifications on page 79-82 and 83-89 respectively of the HNIP Application Guidance.

Please note that applicants must submit their own financial model alongside an application, failure to do so will result in a clarification and may delay the assessment process.

HNIP IRR CALCULATION

Applicants should follow the requirements of the Application Guidance (Appendix E) when calculating their pre-intervention and post-intervention IRRs for the purposes of calculating the Project Funding Gap. Please note, in particular:

- the pre- and post-intervention IRR should be the Real Pre-tax Project IRR;
- the cashflows used to calculate the IRR should exclude general price inflation (CPI/RPI) but may include any under-or over-indexation (e.g. where costs are expected to decrease or increase over time excluding the effects of general inflation);
- where such real price inflation adjustments are made the applicant should reflect such movements in their heat price escalation; or where it is envisaged that part or all real price cost inflation will not be passed onto a customer a clear rationalisation of this should be provided as part of the application;
- the cashflows should exclude all taxes (including business rates);
- the cashflows should exclude financing costs
- the cashflows used for the IRR calculation should have a 40 year time period to be consistent with the FEAM data; and,
- the IRR calculations should be consistent for the pre-intervention and post-intervention IRRs, and the post-intervention IRR should match the hurdle IRR stated in the Application/Funding Plan.

Support in compiling the stage two financial model information is available from the Business Development Managers (BDMs). Get in touch with enquiries@tp-heatnetworks.org for further information.