

Subsidy Advice Unit Report on the proposed Social Housing Decarbonisation Fund Wave 3

**Referred by the Department for Energy Security
and Net Zero**

04 July 2024

Subsidy Advice Unit

Part of the Competition and Markets Authority



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1. Introduction

- 1.1 This report is an evaluation prepared by the Subsidy Advice Unit (SAU), part of the Competition and Markets Authority, under section 59 of the Subsidy Control Act 2022 (the Act).
- 1.2 The SAU has evaluated the Department for Energy Security and Net Zero's (DESNZ) assessment of compliance of the third wave of the Social Housing Decarbonisation Fund (SHDF), with the requirements of Chapters 1 and 2 of Part 2 of the Act (the Assessment).¹
- 1.3 This report is based on the information provided to the SAU by DESNZ in its Assessment and evidence submitted relevant to that Assessment.
- 1.4 This report is provided as non-binding advice to DESNZ. The purpose of the SAU's report is not to make a recommendation on whether the scheme should be implemented, or directly assess whether it complies with the subsidy control requirements. DESNZ is ultimately responsible for making the scheme, based on its own assessment, having the benefit of the SAU's evaluation.
- 1.5 A summary of our observations is set out at section 2 of this report.

The referred scheme²

- 1.6 The scheme relates to the third wave of the SHDF, through which DESNZ proposes to allocate £1.21 billion to social housing providers to improve the energy performance of social housing in England (the Scheme).
- 1.7 The Scheme forms part of a wider SHDF programme of funding announced in 2019 that seeks to raise the energy performance of social housing in England below EPC³ Energy Efficiency Rating C (EPC Rating C) up to that level over a 10-year period.⁴
- 1.8 DESNZ explained that the SHDF is a key means to achieve the government's 2017 Clean Growth Strategy⁵ to bring as much social housing as possible to EPC

¹ Chapter 1 of Part 2 of the Act requires a public authority to consider the subsidy control principles and energy and environment principles before deciding to give a subsidy. The public authority must not award the subsidy unless it is of the view that it is consistent with those principles. Chapter 2 of Part 2 of the Act prohibits the giving of certain kinds of subsidies and, in relation to certain other categories of subsidy creates a number of requirements with which public authorities must comply.

² [Referral of the proposed Social Housing Decarbonisation Fund Wave 3 by the Department for Energy Security and Net Zero](#)

³ An Energy Performance Certificate (EPC) shows the energy performance of a property. EPCs use an A-G rating scale based on the modelled energy bill costs of running the building.

⁴ The SHDF is being delivered in waves. Previous Waves includes the [Demonstrator](#), [Wave 1](#), [Wave 2.1](#) and [Wave 2.2 and the total SHDF programme \(for all waves\) is worth £3.8 billion](#).

⁵ [Clean Growth Strategy - GOV.UK \(www.gov.uk\)](#)

Rating C by 2035 where practical, cost effective and affordable, and for all fuel poor⁶ homes to reach this by 2030.

- 1.9 The Scheme will be open to Local Authorities, Combined Authorities, Housing Associations, Arms-Length Management Organisations and registered charities that own social housing. For mixed housing (ie blocks that include both social and non-social housing), applications will be allowed to include up to 30% non-social housing on an infill basis.⁷
- 1.10 The Scheme will be available for any energy efficiency and heating measures compatible with the Standard Assessment Procedure⁸ that will help improve the energy performance of housing, excluding heating systems which are solely fuelled by fossil fuels. Applicants will be expected to focus on measures that will help lower household energy bills and reduce carbon emissions from social housing. This includes, but is not limited to, energy efficiency measures (such as wall, loft and underfloor insulation) and low carbon heating technologies.
- 1.11 All recipients will be eligible to receive up to £7,500 grant funding for energy efficiency measures for each home, averaged across all housing included in the application. An additional £7,500 of grant funding is available for the installation of low carbon heating in housing off the gas grid. Finally, for on gas grid homes, £20,000 of grant funding is available for the installation of low carbon heating (up to 10% of the housing in a bid). Save in respect of the grant of £20,000 for on gas grid homes, grant recipients will be required to provide at least 50% co-funding towards the measures undertaken. There is no limit on the number of social houses in relation to which an applicant can bid for.
- 1.12 There will be two application routes: a Challenge Fund (that must generally include a minimum of 100 social housing properties),⁹ and Strategic Partnerships,¹⁰ reserved for experienced and trusted social housing providers.
- 1.13 The Scheme is expected to open in Summer 2024 and successful bids are expected to be announced in Autumn 2024. It is expected that grant recipients will undertake energy performance improvement works between September 2024 and September 2028.

⁶ Fuel poverty in England is measured using the Low Income Low Energy Efficiency (LILEE) indicator. A household is considered to be fuel poor if it is characterised by both low energy efficiency and low income.

⁷ In some cases, improvement works are required on non-social housing in order to achieve the works in social housing (for instance in blocks of flats with mixed social housing, privately owned, or rented, properties).

⁸ The methodology currently used by the government to estimate the energy performance of homes. It is used to produce an Energy Performance Certificate (EPC).

⁹ Small social housing providers will be encouraged to apply through a consortium.

¹⁰ A simplified application process with greater flexibility for funding recipients in how they deliver projects.

SAU referral process

- 1.14 On 17 May 2024, DESNZ requested a report from the SAU in relation to the Scheme.
- 1.15 DESNZ explained¹¹ that the Scheme is a Scheme of Particular Interest because it allows subsidies to be granted over the value of £10 million as there is no limit to the amount of funding that can awarded to an individual beneficiary from the fund.
- 1.16 The SAU notified DESNZ on 23 May 2024 that it would prepare and publish a report within 30 working days (ie on or before 4 July 2024).¹² The SAU published details of the referral on 28 May 2024.¹³

¹¹ In the information provided under section 52(2) of the Act.

¹² Sections 53(1) and 53(2) of the Act.

¹³ <https://www.gov.uk/cma-cases/referral-of-the-proposed-social-housing-decarbonisation-fund-wave-3-by-the-department-for-energy-security-and-net-zero>

2. Summary of the SAU's observations

- 2.1 The Assessment uses the four-step structure described in the Statutory Guidance for the United Kingdom Subsidy Control Regime (the [Statutory Guidance](#)) and as reflected in the SAU's Guidance on the operation of the subsidy control functions of the Subsidy Advice Unit (the [SAU Guidance](#)).
- 2.2 We consider that DESNZ has conducted a good quality Assessment and has appropriately considered the Scheme's compliance with the subsidy control principles. In particular, the Assessment reflects the following positive features:
- (a) The policy objective under Step 1 is clearly focussed on the Scheme and sets out the context of the wider objectives relating to social housing decarbonisation. It also sets out the scale of expected deployment of the policy through the Scheme.
 - (b) It uses a range of supporting evidence, both quantitative and qualitative in nature (including some data from the previous SHDF Waves, measurement of the outcomes of the energy performance improvement works with and without the Scheme) that broadly support DESNZ's key statements in the Assessment.
 - (c) It relies on the Scheme guidance which contains a number of features ensuring that the Scheme's design limits the subsidy to what is necessary.
- 2.3 We consider that DESNZ should strengthen Principle B of its Assessment. In particular, it should more clearly explain how the level of grant funding awarded will be proportionate to the requirements of individual beneficiaries and whether it will be the minimum necessary required for them to make proposed improvements. It should explain how the Scheme might avoid funding providers who may already be planning to make energy efficiency improvements to their housing stock and/or have the financial capacity to afford improvements.
- 2.4 Our report is advisory only and does not directly assess whether the Scheme complies with the subsidy control requirements. The report does not constitute a recommendation on whether the Scheme should be implemented by DESNZ. We have not considered it necessary to provide any advice about how the proposed scheme may be modified to ensure compliance with the subsidy control requirements.

3. The SAU's Evaluation

3.1 This section sets out our evaluation of the Assessment, following the four-step structure used by DESNZ.

Step 1: Identifying the policy objective, ensuring it addresses a market failure or equity concern, and determining whether a subsidy is the right tool to use

3.2 The first step involves an evaluation of the Assessment against:

- (a) Principle A: Subsidies should pursue a specific policy objective in order to (a) remedy an identified market failure or (b) address an equity rationale (such as local or regional disadvantage, social difficulties or distributional concerns); and
- (b) Principle E: Subsidies should be an appropriate policy instrument for achieving their specific policy objective and that objective cannot be achieved through other, less distortive, means.¹⁴

Policy objectives

3.3 The Assessment sets out that the specific objective of the Scheme is to improve the energy performance of at least 140,000 social homes¹⁵ to at least EPC Rating C.

3.4 Further, the Assessment explains that the policy objective of the wider SHDF is to improve the energy performance of social housing to EPC Rating C or above, which is the most effective way to reduce carbon emissions and reduce fuel bills. It adds that the SHDF will address the market failures and equity objective identified in the Assessment by providing social housing providers with the finances they need to undertake energy performance improvement works, remedying the deficit left by capital constraints and competing priorities faced by social housing providers, thereby enabling the reduction of fuel poverty and carbon emissions in the social housing sector.

3.5 In our view, the policy objective is focussed, relevant and has been clearly explained. The Assessment also helpfully outlines the objectives of the wider

¹⁴ Further information about the Principles A and E can be found in the [Statutory Guidance](#) (paragraphs 3.32 to 3.56) and the [SAU Guidance](#) (paragraphs 4.7 to 4.11).

¹⁵As defined by sections 68-70 of the Housing and Regeneration Act 2008.

SHDF and how it aims to address the identified market failures and equity rationale.

Market failure

- 3.6 The Statutory Guidance sets out that market failure occurs where market forces alone do not produce an efficient outcome.¹⁶
- 3.7 The Assessment sets out that the market failure is the poor energy performance of social housing that contributes to significant carbon emissions. It identifies the following factors that contribute to the identified market failure:
- (a) Negative externalities: the Assessment argues that there are limited incentives for social housing providers to prioritise spending to improve the energy performance of homes and reduce carbon emissions, despite the benefits of decarbonising housing to tenants and the environment.
 - (b) Capital constraints due to regulation: the Assessment notes that capital constraints limit social housing providers' ability to invest in improving the energy performance of social housing, caused by rent controls in the social housing sector and competing demands on providers' budgets.
- 3.8 In our view, the Assessment sets out and explains well the market failure due to the limited ability and incentives of social housing providers to carry out the works necessary to achieve the stated policy objective.

Equity objective

- 3.9 The Statutory Guidance sets out that an equity objective seeks to reduce unequal or unfair outcomes between different groups in society or geographic areas.¹⁷
- 3.10 The Assessment outlines that the SHDF has an equity objective of addressing fuel poverty in the social housing rented sector, and in doing so, reducing the economic disadvantage that tenants in housing with poor energy performance face through higher fuel bills.
- 3.11 In support of its equity objective argument, the Assessment identifies an inequality in terms of fuel poverty between social housing renters and private housing tenants or owner occupiers. It relies on data on the economic demographics of tenants in England that shows the inequality. The Assessment then explains that the SHDF is targeted at reducing economic disadvantage as it will address

¹⁶ [Statutory Guidance](#), paragraphs 3.35-3.48.

¹⁷ [Statutory Guidance](#), paragraphs 3.49-3.53.

inequity through subsidising the energy performance improvement works needed to bring social housing out of fuel poverty.

- 3.12 In our view, the equity objective is well explained including the underlying reason for the stated inequality.

Consideration of alternative policy options and why the Scheme is the most appropriate and least distortive instrument

- 3.13 In order to comply with Principle E, public authorities should consider why the decision to give a subsidy is the most appropriate instrument for addressing the identified policy objective, and why other means are not appropriate for achieving the identified policy objective.¹⁸
- 3.14 The Assessment sets out several options that were considered, commencing with a long list of options which DESNZ considered against certain criteria set out in supporting evidence (including ‘critical success factors’ in line with Green Book Appraisal Guidance). The long list options considered included the grant option (as set out in the Scheme) and the following other options:
- (a) Market regulation, such as strengthening existing minimum energy and heating standards on social housing providers¹⁹ to require minimum EPC Rating C.
 - (b) Energy supplier obligations, such as placing obligations on energy suppliers on top of their obligations already in place.
 - (c) Market based incentives, such as preferential rates on financial products.
 - (d) Tax incentives, such as preferential tax rates, or stamp duty rebates for social housing providers.
- 3.15 The Assessment concludes that these alternative options would negatively impact the financial viability of social housing providers, either by pushing them into an untenable borrowing position or limiting their capacity to build new properties to meet the high demand for social housing. It also concludes that grant funding would deliver energy performance improvement works over a shorter timeframe than changes to market regulation.²⁰ Accordingly, based on the critical success factors, grant funding was chosen as the most appropriate option for achieving the

¹⁸ [Statutory Guidance](#), paragraphs 3.54-3.56.

¹⁹ Social housing providers are currently required to meet a ‘thermal comfort’ criterion defined in the Decent Homes Standard as a dwelling having efficient heating, effective insulation and a rating equivalent to EPC Rating F.

²⁰ See paragraph 3.20.

specific policy objectives of the Scheme (ie, significant carbon savings and meeting fuel poverty targets).

- 3.16 In our view, the Assessment demonstrates that DESNZ considered several policy options (as well as non-subsidy options) for achieving the policy objective which was supported by evidence setting out the criteria against which each option was considered and the advantages and disadvantages of each option.

Step 2: Ensuring that the subsidy is designed to create the right incentives for the beneficiary and bring about a change

- 3.17 The second step involves an evaluation of the assessment against:

- (a) Principle C: First, subsidies should be designed to bring about a change of economic behaviour of the beneficiary. Second, that change, in relation to a subsidy, should be conducive to achieving its specific policy objective, and something that would not happen without the subsidy; and
- (b) Principle D: Subsidies should not normally compensate for the costs the beneficiary would have funded in the absence of any subsidy.²¹

Counterfactual assessment

- 3.18 In assessing the counterfactual, the Statutory Guidance explains that public authorities should assess any change against a baseline of what would happen in the absence of the subsidy (the 'do nothing' scenario).²² This baseline would not necessarily be the current 'as is' situation (the 'status quo') but what would likely happen in the future – over both the long and short term – if no subsidy were awarded.
- 3.19 The Assessment explains that, in the absence of the Scheme, the pace of energy performance improvement works would be slower. This is because social housing providers operate in a constrained funding environment and are likely to prioritise spending their limited resources on developing new stock and building safety works, where there are stronger commercial incentives and legal requirements respectively.
- 3.20 The Assessment notes that, absent the Scheme, there are likely to be some energy performance improvements across the sector as 'providers begin to look towards net zero by 2050', with some occurring as part of providers' routine

²¹ Further information about Principles C and D can be found in the [Statutory Guidance](#) (paragraphs 3.57 to 3.71) and the [SAU Guidance](#) (paragraphs 4.12 to 4.14).

²² [Statutory Guidance](#), paragraphs 3.60-3.62.

maintenance. DESNZ provided some modelling showing that most improvement works would likely be achieved by 2035 in the counterfactual (rather than by 2028 with the Scheme). The assessment also discusses the prospect of a future regulatory standard, but notes that it will not happen in the near future and there is no clear timeline for this. DESNZ also quantified the outcomes of the expected energy performance improvement works, in terms of housing retrofitted to EPC Rating C, volume of carbon dioxide abated, and houses removed from fuel poverty, both with and without the subsidy.

- 3.21 In our view, the Assessment sets out and explains the counterfactual well. Supporting evidence usefully quantifies the expected situation with and without the Scheme and explains the underlying assumptions that it used.

Changes in economic behaviour of the beneficiary

- 3.22 The Statutory Guidance sets out that subsidies must bring about something that would not have occurred without the subsidy.²³ In demonstrating this, public authorities should consider the likely change or additional net benefit.
- 3.23 In support of its assessment of incentivising a change in economic behaviour, DESNZ points to the success of prior waves of the SHDF, that resulted in large-scale capital investment into energy performance improvement works.
- 3.24 Further, the Assessment describes the incentives for social housing providers to co-fund improvement works that will not generate further revenue. It explains that providers' incentive to do so is to reduce rent arrears – by investing in energy efficiency improvements, tenants will reduce consumption and bills, thereby helping them to pay their rent. Furthermore, evidence from DESNZ indicates that social housing providers are positive about the Scheme and have factored intentions to apply for SHDF funding into their financial plans.
- 3.25 In our view, the Assessment explains the change in economic behaviour which the subsidy is expected to bring about. The provision of evidence setting out outcomes from prior Waves is a strength of the Assessment.
- 3.26 The Assessment could further demonstrate why it is appropriate to have the same level of co-funding requirement for all applicants. In particular, given that providers vary in size and financial capacity, it could examine whether smaller providers and providers with lower financial capacity will be able to put forward the required funds for improvement works at this level of co-funding. Further, the Assessment, when considering the incentives for social housing providers to co-fund the

²³ [Statutory Guidance](#), paragraph 3.64.

improvement works, could have better explained whether the prospect of upcoming changes to regulation on minimum EPC Ratings in social housing could act as a potential incentive.

Additionality assessment

- 3.27 According to the Statutory Guidance, ‘additionality’ means that subsidies should not be used to finance a project or activity that the beneficiary would have undertaken in a similar form, manner, and timeframe without the subsidy.²⁴ For schemes, public authorities should also, where possible and reasonable, ensure the scheme’s design can identify in advance and exclude those beneficiaries for which it can be reasonably determined would likely proceed without subsidy.²⁵
- 3.28 The Assessment explains that the ambitious size and timescale of projects means that they are unlikely to have been completed in a similar form, manner, and timeframe without the subsidy, given that funded projects will be larger and take place over a longer period than the energy performance improvement works that may otherwise have taken place if funded solely by social housing providers.
- 3.29 Further, the Assessment states that only capital costs and some ancillary and administrative costs will be covered by the grant. In support of this, it provides good evidence of what it considers are appropriate capital costs.
- 3.30 In our view, the Assessment adequately demonstrates the additionality of the grants. The Assessment could be further strengthened with the inclusion of more information around the checks and balances applied to capital spending, for example, by providing evidence from prior waves of the SHDF on the outcomes of the audit procedures and any clawback mechanisms used (if any).

Step 3: Considering the distortive impacts that the subsidy may have and keeping them as low as possible

- 3.31 The third step involves an evaluation of the Assessment against:
- (a) Principle B: Subsidies should be proportionate to their specific policy objective and limited to what is necessary to achieve it; and

²⁴ [Statutory Guidance](#), paragraphs 3.63-3.67.

²⁵ [Statutory Guidance](#), paragraph 3.66.

- (b) Principle F: Subsidies should be designed to achieve their specific policy objective while minimising any negative effects on competition or investment within the United Kingdom.²⁶

Proportionality

- 3.32 The Assessment states that the £1.21 billion allocated for the Scheme is proportionate to achieve its specific policy objective (to improve the energy performance of at least 140,000 social homes to EPC Rating C). In support of this, the Assessment:
- (a) demonstrates that there remains a significant funding gap between the amount available for the Scheme and the total amount required to reach EPC Rating C in all social housing²⁷ by 2030 and to install low carbon heating in social housing between 2030 and 2050. This funding gap remains significant, even when other relevant Government grants are taken into account; and
 - (b) explains that, for homes improved under the Scheme, a minimum of 50% co-funding will be required from grant recipients²⁸ and that there is an average base grant funding cost cap per home. The co-funding requirement is intended to provide adequate incentive for social housing providers to apply for funding, whilst disincentivising over bidding and ensuring that cost-effective work is undertaken. The Assessment explains that the required co-funding level and the average cost cap are based on data from previous waves of the SHDF.
- 3.33 The Assessment further considers how various elements of the Scheme design help to minimise the size of the subsidy, including those elements contained in the Grant Funding Agreement (GFA) such as key performance indicators, the clawback mechanism, and ongoing period reviews of the Scheme.
- 3.34 In our view, the Assessment provides a well evidenced explanation of the proportionality of the Scheme, drawing on data from the previous SHDF Waves.
- 3.35 The Assessment should more clearly explain how the levels of grant funding will be proportionate to the requirements of individual beneficiaries and whether it will be the minimum necessary required for them to make proposed improvements. In particular, it should explain how the Scheme might avoid funding providers who

²⁶ Further information about the Principles B and F can be found in the [Statutory Guidance](#) (paragraphs 3.72 to 3.108) and the [SAU Guidance](#) (paragraphs 4.15 to 4.19).

²⁷ Currently around 1.2 million social housing properties are rated below EPC Rating C.

²⁸ With the exception of 10% of homes per bid that are on the gas grid (see above at paragraph 1.11).

may already be planning to make energy efficiency improvements to their housing stock and/or have the financial capacity to afford improvements.

- 3.36 The Assessment should also explain why there is no co-funding requirement for the £20,000 funding available for low carbon heating (for up to 10% of social housing per bid) that are on the gas grid.
- 3.37 Finally, the Assessment could include evidence of the expected volumes (as opposed to the maximum volume) of non-social housing improved (by, for example, drawing on evidence from past waves) and the impact of these volumes on how the Scheme remains proportionate to its policy objective.

Design of subsidy to minimise negative effects on competition and investment

- 3.38 The Assessment provides details on most of the subsidy characteristics set out in Chapter 3 of the Statutory Guidance. The Assessment notes that the subsidy design mitigates negative effects on competition or investment due to a number of factors, including:
- (a) the size of the subsidy is low compared to total spending by social housing providers;
 - (b) the subsidy will be limited to 50% of total project cost;
 - (c) the Scheme is open to all social housing providers;
 - (d) funding will be allocated to all providers that achieve the minimum standard (so the allocation of funding should not be limited to a small number of large, high-quality bids); and
 - (e) the Scheme will run for a clearly defined period of time.
- 3.39 In our view, the Assessment closely follows the Statutory Guidance, identifying a number of relevant subsidy characteristics and appropriately assessing how they might minimise any negative effects of the Scheme on competition and investment.

Assessment of effects on competition or investment

- 3.40 The Assessment explores the impact of the Scheme on competition in relation to markets most likely to be affected by the Scheme: the social housing market, the private housing sector (either private-owner occupied or rental market) and the retrofit sector.

- 3.41 In relation to the social housing market, the Assessment acknowledges that the Scheme will confer an economic advantage on beneficiaries as they will receive financial assistance from DESNZ. In particular, the Scheme will primarily enable social housing providers to improve the quality of their housing stock. The Assessment explains that the Scheme is expected to have minimal impact on competition due to:
- (a) The 'vast' lack of social housing supply relative to demand.
 - (b) The restrictions on rent increases: social housing providers are unlikely to increase rents on housing that has benefited from improvements funded through the Scheme. This is because rent increases are limited to the maximum percentage allowed by the Regulator of Social Housing, and typically most providers already increase rents by the maximum allowed.
 - (c) The fact that social housing providers are unlikely to dispose of improved properties to the private housing sector. Due to the significant shortage of social housing in the sector it is expected that social housing providers will avoid selling stock wherever possible. The Assessment notes that historically there are very low levels of sales of social housing into the private sectors and that the vast majority of these sales occur only where this is required pursuant to the Right to Buy scheme.²⁹ It also highlights evidence from an independent report which indicates that social housing providers have a preference to retain properties which have an EPC Rating of at least C.
- 3.42 In relation to the private housing sector, the Assessment explains that the improvement of non-social housing, through infill (see paragraph 1.9 above), should be kept to the absolute minimum required and limited to situations in which social housing would be adversely affected without it.³⁰ The Assessment notes that the number of non-social houses improved is limited to a maximum 30% of homes for each bid. It further explains that even if the maximum possible proportion of non-social housing were treated under the Scheme, this would represent a very small percentage of the private housing sector and, as a consequence, any impacts on these markets is likely to be very small.
- 3.43 Finally, in relation to the retrofit sector, the Assessment states there is a 'small' risk that the increased demand on this sector from the Scheme could lead to inflation of prices of labour or other inputs in the sector.³¹ In addition, it notes that there

²⁹ The Right to Buy scheme allows most council tenants to buy their council home at a price lower than the full market value.

³⁰ For example, cases where social housing would not be able to meet EPC Rating C without works taking place on non-social housing, bearing in mind reasonableness and cost effectiveness.

³¹ Particularly for workers who are TrustMark Registered and are therefore qualified to carry out retrofits for government schemes.

were some increases in price of relevant inputs in the supply chain during the previous SHDF Waves. However, the Assessment concludes that there will be the necessary skilled labour available and that the market will be able to deliver the Scheme without significant supply chain issues. To support this conclusion, the Assessment points to growth in employment in the retrofit sector, investment in the training of skilled labour and also the fact that work on previous SHDF Waves will end in March 2026 and will free up capacity in the supply chain. It also argues that any rise in the prices of relevant products have been mainly down to wider economic circumstances, rather than spending funded under previous waves of the SHDF.

- 3.44 In our view, the Assessment clearly explains why the impact of the Scheme on competition will be limited. It addresses the main markets where the impact of the Scheme is likely to be felt and presents credible evidence to support the conclusion that the competition impacts are likely to be limited. However, the Assessment could more clearly consider the impact of the Scheme on the social housing providers' incentive to sell improved homes into the private housing sector, including why it considers that those future sales would be limited (for example, by demonstrating how the aims and objectives of social housing providers might limit their incentive to sell the housing that has been improved).³²

Step 4: Carrying out the balancing exercise

- 3.45 The fourth step involves an evaluation of the assessment against subsidy control Principle G: subsidies' beneficial effects (in terms of achieving their specific policy objective) should outweigh any negative effects, including in particular negative effects on: (a) competition or investment within the United Kingdom; (b) international trade or investment.³³
- 3.46 The Assessment sets out the key benefits of the Scheme in relation to the specific policy objective of improving the energy performance of at least 140,000 social homes in England to EPC Rating C or above, to reduce carbon emissions and reduce fuel bills, quantifying these where appropriate.
- 3.47 The Assessment considers the potential negative impacts of the Scheme on competition in the private housing sector as set out in paragraphs 3.42 and 3.44 above, and in relation to the retrofit sector as set out above in paragraph 3.43.

³² The Assessment also does not consider whether improvements to social housing could have an impact on demand by social renters for private rented housing. However it explains that any impact is likely to be very small given, amongst other things, the already long waiting lists for social housing and that by definition social housing is rented at large discount to market rental prices.

³³ See [Statutory Guidance](#) (paragraphs 3.109 to 3.117) and [SAU Guidance](#) (paragraphs 4.20 to 4.22) for further detail.

- 3.48 The Assessment explains that DESNZ do not consider the Scheme to have an impact on international trade and investment as all installers are required to be in the UK to carry out the work. In addition to this, the Assessment explains that the geographical distribution impacts will be reviewed on a case-by-case basis prior to any funding being granted. The Assessment concludes that the expected benefits of the Scheme outweigh the potential negative impacts.
- 3.49 In our view, the Assessment demonstrates that DESNZ has considered the expected benefits of the Scheme and its potential negative effects in line with the Statutory Guidance. The Assessment could have more explicitly considered the estimated value of these benefits and how it compares with the potential negative impacts on competition and investment. We note that the Assessment could have been strengthened by including or referencing the calculation of the benefits set out in the supporting evidence (ie, the Outline Business Case).

Energy and Environment Principles

- 3.50 This step involves an evaluation of the Assessment with regard to compliance with the energy and environment principles, where these are applicable to the Scheme.³⁴
- 3.51 The Statutory Guidance summarises the scope of the different energy and environment principles that apply to different types of subsidies.³⁵ DESNZ has carried out an assessment of the Scheme against Principles A and B, and has provided reasons why it considers Principles C, D, E, F, G, H and I not to be applicable to the Scheme.

Principle A: Aim of subsidies in relation to energy and environment

- 3.52 The assessment against Principle A should show how the subsidy is consistent with delivering a secure, affordable and sustainable energy system and a well-functioning and competitive energy market, or increasing the level of environmental protection compared to the level that would be achieved in the absence of the subsidy. If a subsidy is in relation to both energy and environment, it should meet both of these limbs.³⁶

³⁴ See Schedule 2 to the Act.

³⁵ Principles A and B apply to all subsidies in relation to energy and environment. Principle C applies for subsidies for electricity generation adequacy, renewable energy or cogeneration. Principle D applies to subsidies for electricity generation only. Principle E applies to subsidies for renewable energy or cogeneration. Principle F applies to subsidies in the form of partial exemptions from energy related taxes and levies. Principle G applies to subsidies that compensate electricity intensive users for increases in electricity costs, Principle H relates to subsidies for decarbonisation of industrial emissions. Principle I relates to subsidies for improving energy efficiency of industrial activities.

³⁶ [Statutory Guidance](#), paragraphs 4.19-4.28.

- 3.53 The Assessment states that the Scheme relates to both energy and the environment, and that both the limbs of Principle A are met.
- 3.54 In relation to the first limb, the Assessment states that social housing treated under the Scheme will require less energy thus placing less demand on the energy system. The Assessment goes on to explain that this will contribute to a sustainable, well-functioning and competitive energy market though reduced need for fossil fuels, gas and electricity networks.
- 3.55 In relation to the second limb, the Assessment states that through incentivising the installation of energy efficient and clean heat measures, the Scheme will result in an increased level of environmental protection through the reduction of greenhouse gas emissions. The Scheme is a part of the UK's net zero plan to reduce carbon emissions and its specific policy objective also promotes this, making it consistent with Principle A.
- 3.56 In our view, this sufficiently explains how the Scheme complies with Principle A.

Principle B: Subsidies not to relieve beneficiaries from liabilities as a polluter

- 3.57 The assessment against Principle B should explain clearly how the proposed subsidy or scheme does not relieve a polluter from having to bear the full costs of the pollution caused.³⁷
- 3.58 The Assessment states that the Scheme will have a positive impact on the environment through the reduction of carbon emissions of social housing. In addition to this, the GFA will set out that subsidies made under the Scheme will not relieve the beneficiary from liabilities arising from its responsibilities as a polluter under the law.
- 3.59 In our view, this sufficiently explains how the Scheme complies with Principle B.

Other Requirements of the Act

- 3.60 This step in the evaluation relates to the requirements and prohibitions set out in Chapter 2 of Part 2 of the Act, where these are applicable.³⁸ DESNZ has identified that a subsidy under this Scheme would involve the delivery of a subsidy that involves Services of Public Economic Interest (SPEI) and is therefore subject to conditions. DESNZ has identified that a subsidy given under the Scheme is for the benefit of the public in the form of social housing stock with improved energy

³⁷ [Statutory Guidance](#), paragraphs 4.29-4.35.

³⁸ [Statutory Guidance](#), chapter 5.

performance, reduced carbon emissions and reduced fuel poverty and therefore amounts to a Service of Public Economic Interest (SPEI).³⁹

- 3.61 Consequently, DESNZ has assessed whether the requirements of Section 29 of the Act would be complied with in relation to any subsidy given under the scheme.

The subsidy is limited to what is necessary to deliver the SPEI services having regard to costs of delivery and reasonable profits⁴⁰

- 3.62 Although this requirement is not addressed directly, DESNZ explains elsewhere in the Assessment that the Scheme ensures that the support given is limited to what is necessary by putting various design controls such as competitive bid processes, cost-caps, co-funding, clawback, and monitoring requirements in place.

The subsidy is given in a transparent manner, meaning that the subsidy is given in accordance with a written contract (or other legally enforceable arrangement in writing), which sets out the terms of the subsidy and certain prescribed information⁴¹

- 3.63 The Assessment explains that where grant funding is awarded, successful applicants will be required to sign a Grant Offer Letter (GOL), GFA and a Data Sharing Agreement (DSA) so that payments can be made.
- 3.64 In our view, the Assessment could be improved by setting out the proposed terms of the GOL, GFA and/or DSA which ensure that the requirements of Section 29 of the Act are met.

Arrangements are in place to regularly review the subsidy to ensure it remains limited to the minimum necessary and that any excess funds can be recovered⁴²

- 3.65 The Assessment states that DESNZ will keep the SPEI funding under regular review during the delivery period and the conclusion of project delivery to ensure that it is spent on the agreed services.
- 3.66 In the SAU's view, the Assessment provides a reasonable explanation of the arrangements in place to ensure that the Scheme is limited to the minimum necessary and that any excess funds can be recovered. As set out above, the

³⁹ The Assessment explains that these services would not be provided on the terms required by an enterprise under normal market conditions as social housing providers would not be able to finance energy performance improvements required to reduce carbon emissions and bring tenants out of fuel poverty.

⁴⁰ Section 29(2) of the Act.

⁴¹ Section 29(3)-(5) of the Act.

⁴² Section 29(6) of the Act.

Assessment could be improved with the provision of information as set out in paragraph 3.35 to 3.37.

4 July 2024