
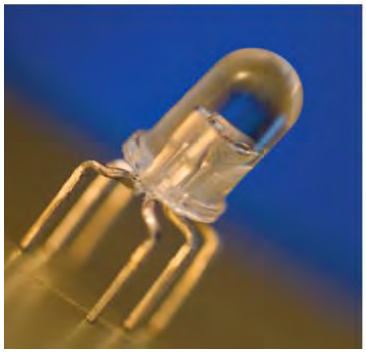


Assessment of climate change policies as part of the European Semester

Country Report Latvia

21 January 2015

A report submitted by ICF Consulting Services
in association with

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to DG Climate Action

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Contents

1 Short Summary

After multiple suspensions Latvia's electricity market was liberalized on 1 January 2015, gradual liberalization of the gas market is planned until April 2017. To improve Latvia's security of energy supply, two electricity interconnection projects and one gas underground storage facility modernisation project are going to be implemented until 2020.

By 2020, Latvia can increase its emissions not covered by the EU ETS by 17% compared to 2005, according to the Effort Sharing Decision (ESD). The latest data for 2013 show that Latvia emitted 8.5 percentage points less than it was allowed under the annual allocation interim target under the ESD for the year 2013. National projections indicate that the country will miss its 2020 target by about 1.5 percentage points with existing measures but will meet the target with additional.

The key policy developments in the last year (Jan. 2014 – Jan. 2015) include the amendment of the Energy Market Law aiming to open Latvia's electricity market, as well as amendment of the Energy Law (see Chapter. 4.2.3). A detailed energy policy framework – Guidelines of Energy Development for 2014 to 2020 - are currently being developed and an informative report on Financing of Energy Policy in the period from 2014 to 2020 was approved by the Ministry of Economics. On 1 January 2014, a new Law on a Tax for Subsidized Electricity was introduced (see Chapter 4.2.1).

2 Climate and energy policy priorities

Latvia has not yet implemented a comprehensive climate change strategy, as the key concern in the country is still energy security. Latvia is dependent on energy imports and remains isolated from the EU energy networks. The national Energy Strategy 2030 (Enerģētikas stratēģija 2030), in force since March 2013, sets long-term actions to ensure energy supply, competitiveness, energy efficiency, and the use of renewable energy (Cabinet of the Ministers, 2013a). In May 2014, an informative report on financing of energy policy in the period from 2014 until 2020 (Par enerģētikas politikas finansēšanu laika posmā no 2014.-2020.gadam) was introduced. According to the report, the main tasks until 2020 are: liberalization of the electricity and gas market, introduction of support scheme for low-income residents, modernisation of energy infrastructure and interconnection projects, development of subsidy programme for renewable energy sources and elaboration of energy efficiency strategy (Cabinet of the Ministers, 2013b). Furthermore, on 12 December 2014 Guidelines of Energy Development for 2014 to 2020 (Enerģētikas attīstības pamatnostādnes 2014. - 2020. gadam) was published for public debate by the Ministry of Economics. According to the guidelines as a long term energy sector planning document, the main objectives for the energy sector in the period until 2020 are to increase energy security and promote sustainable energy (Latvian Ministry of Economics, 2014a).

In 2012, Latvia had the second highest RES share in the EU28, with 36.6%, achieved largely by historically important hydropower and followed by biomass (Latvian Ministry of Economics, 2014a). The main renewable energy support scheme, a feed-in tariff, is still under revision and a draft Renewable Energy Law (Atjaunojamās enerģijas likums) passed by the Latvian Parliament is awaiting its adoption. However, a new tax on subsidized renewable energy was introduced in January 2014. According to the Law On Taxation of Subsidized Electricity (Subsidētās elektroenerģijas likums), the tax rate from 5% to 15% should be paid by companies receiving financial support for power generation from renewable energy sources or from Combined Heat and Power (CHP) plants (Saeima, 2014a). The planned revenue from the tax for the period 2014 – 2017 is approx. 150 million EUR (MUREII, 2014a). According to the stakeholders concerned, the tax is having an adverse impact on the economic case for renewables deployment in Latvia. The tax is not only hindering the development of new RES-E projects in Latvia, but could also be crucial for survival of the existing companies (Keep on Track, 2014).

From January 2015 the amended Energy Market Law (Elektroenerģijas tirgus likums) opened Latvia's end-user electricity market. In order to reduce price rise risks for poor households, Latvia's parliament approved a support programme with the aim of compensating low-income earners and families with

three and more children for the electricity price growth (Saeima, 2013a). Furthermore, it is planned to liberalize the gas market of Latvia until April 2017 (Saeima, 2014b).

Although improving energy efficiency is one of the priorities of Latvia with an overall budget of 500 million EUR until 2015 for different subsidy tenders, the planed development of a long-term energy efficiency strategy and a detailed action plan have been postponed. However, a Draft Law on Energy Efficiency (Energoefektivitātes likums) was developed in 2014 and submitted to the Parliament for consideration. The law aims to ensure greater energy efficiency in energy production, distribution and final consumption. Furthermore, it sets mandatory energy audits for large companies. As well as promotes development of the energy market and creation of a national energy efficiency fund. The law shall ensure implementation and monitoring of the national energy efficiency action plans, which are to be elaborated every third year (Latvian Ministry of Economics, 2014b).

Although gradual liberalization of the gas market is foreseen until April 2017, gas import dependence in Latvia remains extremly high (96%) (ECFIN). To improve Latvia's security of energy supply, the country is diversifying its supply routes through more interconnection and also seeks to enhance gas storage to increase buffers from shocks. Two electricity interconnection projects - "Kurzeme Ring" third interconnection and the third Latvian-Estonian transmission network interconnection project, as well as Inčukalns underground gas storage facility modernisation and expansion project currently being developed (Latvijas Gaze, Latvenergo).

3 GHG trends and projections

Latvia reduced its total GHG emissions by 2% between 2005 and 2013; these reductions only happened in the last two years. The share of GHG emissions not covered by the European Emission Trading Scheme (EU ETS) is around 76%, which is above the EU28 average (see Table 1).[1]

Table 1 Key data on GHG emissions

		National data				*EU28*
		2005	**2011**	**2012**	**2013**	***2013***
Total GHG emissions	Mt CO_2eq	11.1	11.1	11.0	10.9	*4 539*
Non-ETS emissions	Share in total emissions	74%	74%	75%	76%	*58%*

Source: EEA 2014a; EEA 2014c

By 2020, Latvia can increase its emissions not covered by the EU ETS by 17% compared to 2005, according to the Effort Sharing Decision (ESD). The latest data for 2013 show that Latvia emitted 8.5 percentage points less than it was allowed under the annual allocation interim target under the ESD for the year 2013 (see figures in Table 2). National projections indicate that the country will miss its 2020 target by about 1.5 percentage points with existing measures (WEM) but will meet the target with additional measures (WAM) (EEA 2014a).

Table 2 Non-ETS emission targets, trend and projections

		Compared to base year
2013	ESD interim target	+ 9.5%
	ESD emissions	+ 1.0%
2020	ESD target	+ 17.0%

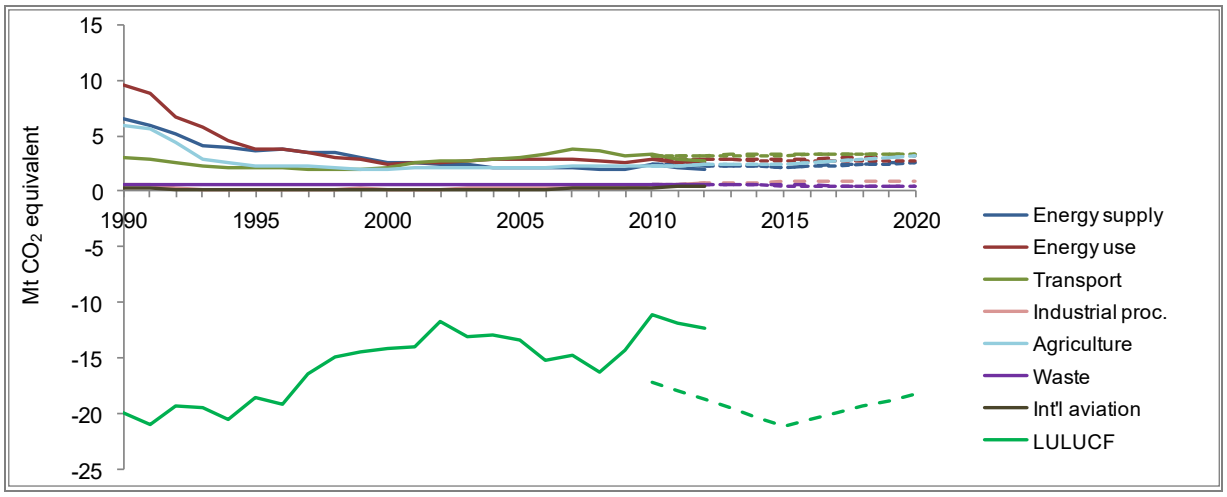
[1] The European Environment Agency has developed a complex methodology to measure progress on the Non-ETS/ESD targets of all EU Member States. This report uses the figures derived on this basis. A detailed explanation and the underlying absolute amounts are contained in Annexes 1-3 of the EEA report No 6/2014 "Trends and projections in Europe 2014. Tracking progress towards Europe's climate and energy targets for 2020" available at http://www.eea.europa.eu/publications/trends-and-projections-in-europe-2014/

	ESD projections WEM	+ 18.5%
	ESD projections WAM	+ 14.8%

Source: EEA 2014a. Green indicates target met or exceeded, orange indicates a value below.

GHG emissions from energy industries, energy use, the agricultural and the transport sectors are almost equivalent and are projected to remain relatively stable until 2020 (see Figure 1 below for historic and estimated emissions by sector). Only agriculture is projected to increase slightly.

Figure 1 GHG trends and projections by sector



Source: EEA 2014a. Actual data until 2012 and projections from 2010 onwards.

4 Policy development

This section covers significant developments made in key policy areas between January and December 2014. It does so through two different perspectives: 1) progress on the policies communicated under the National Reform Programme 2) developments in the identified national priority sectors and policy areas.

4.1 Key policies as outlined by the National Reform Programme

Member States prepare National Reform Programmes (NRPs) each April outlining the country's progress and the key policies and measures to achieve targets under the EU 2020 Strategy. These key policies and measures are summarised in the following table and their current status is provided.

Table 3 Key policies and measures as outlined by the NRP 2014

Law on Tax for Subsidized Electricity	
Status in the NRP	In force
Status as per Dec 2014	In force. In place for the period from 1 January 2014 to 31 December 2017.
Description of policy	See Chapter 4.2.1.

Amendments of Natural Resource Tax and Excise Duty Tax	
Status in the NRP	In force
Status as per Dec 2014	Both in force since 1 January 2014.
Description of policy	See Chapter 4.2.1.

Law on Energy Performance of Buildings	
Status in the NRP	In force since 9 January 2013.
Status as per Dec 2014	In force.
Description of policy	The Law on Energy Performance of Buildings establishes minimum building performance requirements as well as certification requirements for energy, heating and air-conditioning in buildings (Saeima, 2013b).

Projects for increasing energy efficiency	
Status in the NRP	Next round of the subsidy programme “Increase of the efficiency of district heating systems” and a new subsidy programme “Support for Introducing Green Technologies in Production” planned in 2014.
Status as per Dec 2014	Sixth round of the subsidy programme “Increase of the efficiency of district heating systems” was open for new submissions from 15 September 2014 until 14 November 2014, the new subsidy programme “Support for Introducing Green Technologies in Production” was open for aplications from 21 January 2014 until 20 March 2014
Description of policy	See Chapter 4.2.2.

Amendments to the Electricity Market Law	
Status in the NRP	Amendments to the Electricity Market Law will come into force on 1 January 2015.
Status as per Dec 2014	In force from 1 January 2015.
Description of policy	The amended Electricity Market Law regulates the opening of the electricity market for households from January 2015 within Baltic Energy Market Interconnection Plan and sets a support mechanism for needy and low-income households to compensate the rise in expenses on electricity after the cancellation of the Start-tariff. See Chapter 4.2.3.

Amendments to the Energy Law	
Status in the NRP	In force since 13 March 2014.
Status as per Dec 2014	In force.
Description of policy	See Chapter 4.2.3.

Introduction of net-metering	
Status in the NRP	In force since 1 January 2014.
Status as per Dec 2014	In force.
Description of policy	The net-metering scheme introduced by the Ministry of Economics is in force since January 2014. The scheme applies to clients who are at the same time producers of electricity and are connected to the electricity grid through a connection with a throughput value smaller than or equal to 11kW. Producers can apply for an offer from the responsible grid operator for supplying electricity to the grid and are required then to pay a grid use charge (Latvian Ministry of Economics, 2014c).

4.2 National policy priorities

The sub-sections below provide updates on key existing and new policies in priority sectors and policy areas of relevance to the energy and climate targets under the Europe 2020 strategy[2]. Each sector or policy area contains information on the most important policy instruments in operation or development.

4.2.1 Environmental Taxation

In Latvia the implicit tax rate on energy is the fifth lowest in the EU with EUR 70 per ton of oil equivalent in 2012 (Eurostat, tsdcc360). However, the share of environmental tax revenues in overall tax revenue was 8.7% in 2012 and therefore above the EU average of 6.1% (Eurostat, ten00064). When comparing environmental tax revenues with GDP, Latvia is close to the EU average with 2.4% in 2012 (Eurostat, ten00065).

Aiming to avoid an increase of the component of feed-in payment for renewable energy sources (RES) in the total price of electricity, on 1 Jaunary 2014 a Law On Taxation of Subsidized Electricity (Subsidētās elektroenerģijas likums) was introduced by the Cabinet of the Ministers. The tax is paid by companies that receive financial support for power generation from renewable energy sources or from Combined Heat and Power (CHP) plants. According to the Law, the tax is applied to the taxable income from the selling of the produced electricity within the framework of the mandatory procurement or receiving guaranteed payment for the electric capacity installed. The following tax rates are stated: 15% - for the electricity produced using fossil fuels, 10% - the electricity produced utilising renewables, and 5% reduced rate for high efficiency CHP units in exceptional cases with the aim to limit the direct effect on end-user's heat energy price. The tax is a temporary one and is scheduled to be in place until 2018, however, there is the possibility that it might be reduced or even abolished beforehand in the case of reduced subsidies under the framework of mandatory procurement [3] (Saeima, 2014a). The total state budget income from the tax for the period 2014 – 2017 is expected to be approx. 150 million EUR. The revenue is flowing into the budget of the Electricity Customer Support Fund, which provides support for low-income households to avoid electricity poverty (MUREII, 2014a, see Chp. 4.2.6).

Latvia has a longstanding natural resource tax (Dabas resursu nodoklis) that charges fees on air pollution, landfilling, extraction of natural resources and greenhouse-gas emissions produced by stationary technological equipment not included in the emission quotas. Taxes are also charged on goods polluting water and environmentally harmful goods. According to the amendments of the

[2] The Consortium jointly with DG Clima identified these based on identified challenges in Country Profiles (EEA, 2014), share of sectors in total GHG emissions, and Country Specific Recommendations (2014). DG Clima has identified additional relevant issues to be reviewed for some or all Member States, including country specific energy challenges.

[3] Mandatory procurement component is a support scheme for electricity produced from RES and electricity produced in cogeneration. The procurement price depends on the type of renewable sources.

Natural Resources Tax, in force since January 2014, a number of new natural resource tax objects have been introduced, as well as tax rates have been increased. The tax rate for the use of water resources for production of electricity in a hydroelectric power plant (<2 MW), shall be 0.00853 EUR per 100 m3 of the water that has flown through the hydrotechnical structure. Increased tax rate on municipal waste landfill - 12 EUR per tonne (previously 9.96 EUR). Higher payment will be referred to environmentally harmful goods, packaging and vehicles covered by the Law on Used Vehicles. For the first time in Latvia registered vehicle tax rate increased from 31.30 EUR to 40 EUR (Saeima, 2014c).

According to the amendments to the Excise Duty Law (Likums par akcīzes nodokli) made on 27 November 2013 by Latvian Saeima, excise duty taxe rate for petroleum gas increased from 128,06 EUR to 161 EUR per 1000 kilograms beginning from Jaunary 2014. The tax rate of 5.65 EUR per 1000 m3 applies to natural gas used as fuel for industrial production and initial processing of raw materials for agricultural needs (Saeima, 2013c).

4.2.2 Energy Efficiency

Within the EU28, Latvia has the sixth most energy-intensive economy. Energy intensity declined by 7% from 2005 to 2012 (Eurostat, tsdec360). Final energy consumption remained constant between 2005 and 2012 mainly due to increases in the industrial, service and agricultural sectors that could not be absorbed by reductions in the residential and transport sectors. Thus, Latvia is one of the seven EU MS that did not reduce their final energy consumption at all (Eurostat, tsdpc320). However, Latvia has EU energy efficiency targets that allow for a limited increase in consumption over historic levels and it is, therefore, currently on track towards meeting the targets (EEA, 2014a).

The Ministry of Economics planed to develop a long-term energy efficiency strategy and a detailed action plan in the first half of 2014. Elaboration of both documents has been postponed, however a Draft Law on Energy Efficiency (Energoefektivitātes likums) was developed in 2014 instead and submitted to the Parliament for consideration, but it has not been adopted yet. The law aims to ensure energy efficiency in energy production, distribution and final consumption. Furthermore, it defines regular, mandatory energy audits for large companies. It is also meant to promote further development of the energy market and create a national energy efficiency fund. The law shall ensure the implementation of the national energy efficiency action plan (Latvian Ministry of Economics, 2014b).

On 15 September 2014 the sixth round of the subsidy programme “Increase of the efficiency of district heating systems” was opened for new submissions. Investment support was available for: a) construction and reconstruction of heat source, transmission and distribution system, including technological equipment purchase and installation; b) preparation of project documentation. The overall available budget for the programme amounted to 14,196,678.02 EUR. The maximum subsidy per project was 8,537,230 EUR. The tender was open for submissions until 14 November 2014. The programme is administered by the Investment and Development Agency of Latvia (LIAA) (LIAA, 2014a).

On 21 January 2014, the LIAA announced a new subsidy programme, “Support for Introducing Green Technologies in Production” within the Norwegian Financial Mechanism 2009 – 2014 programme “Green Industry Innovation”. The tender was open for applications from 21 January 2014 until 20 March 2014. The overall budget of the programme was 7,769,107 EUR. Grants per project ranged from 170,000 EUR to 700,000 EUR, with aid intensity at 45%. The aim of the tender was to support the introduction of innovative environmental technologies, services or products within the following eligible measures: production of renewable energy; production of green (energy efficient) products and materials for buildings; clean transportation; water management; waste management; ecodesign; any other improvements in products, technologies or processes in other fields, contributing to energy efficiency, lower emissions or lesser consumption of resources (LIAA, 2014b).

4.2.3 Energy Networks

67 million EUR co-financing were granted by the EU for “Kurzeme Ring” third interconnection and the third Latvian-Estonian transmission network interconnection project. "Kurzeme Ring" is part of the larger "NordBalt" project, which implements the installation of the Latvia-Estonia-Sweden interconnection, aimed at improving power supply reliability in the Baltic region. The second successful project, the Latvian-Estonian transmission network interconnection project, shall eliminate

the overload of the existing electrical supply networks in Latvia and Estonia. Moreover, once implemented, it shall open the EU electricity market for both countries. The Latvian-Estonian transmission network interconnection project is expected to be operational by 2020 (Baltic Course, 2014a).

Furthermore, the first stage of modernisation and reconstruction of the Inčukalns underground gas storage facility with overall budget of 89 million EUR is planned to be implemented by 2018. It foreseess reconstruction of drilling, collection points as well as the installation of a new compressor. The modernisation should increase security and storage of natural gas extraction capacity will grow from 30 million m3 per day to 32 million m3 per day (Latvijas Gaze).

Since January 2015 Latvia's electricity market is completely liberalized, meaning that 850,000 households are able to buy energy directly on the market (Saeima, 2014c). Those consumers who do not wish to change their provider are not required to review their current contracts. Electricity tariffs are no longer regulated, and traders can offer consumers different options. Consumers can choose the most beneficial options in terms of prices. The Public Utilities Commission is serving as a regulator and is responsible for evaluating and approving tariffs and approving a mandatory procurement component. Any electricity trader is allowed to work in the free market. Since January 2015 traders are allowed to provide other services along with supply of electricity that include, for instance, telephone communications, internet, television, and electricity. Thus residents save money on commission payments for other services and receive an altogether better offer (Latvian Ministry of Economics, 2014b; BNN).

In order to reduce price rise risks for poor households, the 2014 state budget included the allocation of 3.2 million EUR for price rise compensation. On 18 September 2014, Latvia's parliament approved amendments to the Electricity Market Law with the aim to compensate low-income earners and families with three and more children for electricity price growth. These households are called "protected consumers" and part of their costs for the electricity will be subsidised. In 2015, low-income residents will have to pay 0.1164 EUR for 100 kilowatt-hours a month, whereas large families will be able to pay the same price for up to 300 kilowatt-hours per month (The Baltic Course, 2014a).

On 20 February 2014, the Latvian parliament, Saeima, approved amendments to the Energy Law (Enerģijas likums), envisaging gradual liberalization of the gas market until April 2017. Based on the amendments, the market could be opened earlier if gas distribution system will be connected to EU-network or the assertive supplier's share is smaller than 75%. At the moment, the only company buying, storing, transporting, distributing and selling natural gas in Latvia is "Latvijas Gaze". Russia is the sole supplier of natural gas to Latvia and Latvia's natural gas supply system is only connected with Lithuania and Estonia (Baltic Course, 2014c).

4.2.4 Transport

GHG emissions as well as energy consumption from transport decreased slightly between 1990 and 2012. However, the proportion of transport emissions in Latvia's total emissions has increased to 25%, well above the EU average of 20%. Average emissions for newly registered cars are very high in Latvia with a level of 147.1 CO_2/km in 2013. The level is the highest in the EU and has decreased by 21% between 2005 and 2013, at a slower rate than the EU average of 22% (Eurostat, tsdtr450). Fuel taxation in Latvia is below EU average. The road fuel excise duties on petrol are the fourth lowest among EU MS and the excise duties on diesel are the eighth lowest (EEA, 2014b).

In Latvia vehicle taxes are only partly based on CO_2 emissions. The registration tax is calculated according to CO_2 emissions. In addition, a natural resource tax is levied on every vehicle. The ownership tax in Latvia is based on maximum gross weight for passenger cars and commercial vehicles (ACEA 2014, 2012). Latvia does not charge any tolls for road use (CE Delft, 2012).

The Law on the Toll for the Use of Motorways in force from January 2014 foresees a tax for the use of the motorway by transport vehicles (mass < 3500kg), which are only intended for the carriage of goods by road. The toll shall be paid according to the emission level of the vehicle's engine and the number of vehicle's axles, yearly rates range from 427 to 925 EUR (Saeima, 2014d).

On 2 February 2014, Ministry of Environmental Protection and Regional Development announced a new call for proposals under the subsidy programme "Climate Change Financial Instrument". The

tender was open for applications from 28 February 2014 until 8 April 2014 and the overall budget of the programme was around 5 million EUR. Grants for each project is between 18,500 EUR and 550,000 EUR, with an aid intensity from 35% to 85%. The aim of the tender is to support the deployment of electric vehicles and the charging infrastructure in Latvia. In the first tender of the programme 141 projects with an overall budget of 4,234,921.97 EUR were approved. On 16 October 2014, the vice president of Latvian "Automotive Association", Ingus Rutins, indicated that around 40 electric vehicles have been registered in Latvia in 2014. The majority of these cars are funded from the state budget program "The Climate Change Financial Instrument". The municipalities of Sigulda, Bauska, and Kekava regions each acquired two electric vehicles in 2014 (Ministry of Environmental Protection and Regional Development, 2014a, 2014b; Baltic Course, 2014b).

4.2.5 Agriculture

According to the National Development Plan for 2014 – 2020, Latvia supports agricultural measures that preserve the environment and reduce GHG emissions from agricultural activities. The share of land used for organic farming should increase more than 15 % by 2030 (UNFCCC, 2013; EEA, 2014a).

Regulation No. 834 of the Cabinet of Ministers “Regulation Regarding Protection of Water and Soil from Pollution with Nitrates Caused by Agricultural Activity” from 23 December 2014 determines the requirements and restrictions for the use and land application of different types of fertilizers. Particularly sensitive areas for agricultural activities are subject to stricter requirements. New regulations foresee the same requirements in the use of digestion as in the use of manure. Forthermore, parameters are elaborated, which should be taken into account in the preparation of crop fertilization plans. Also maximum nitrogen norms for different crops, taking into account the fertilizer used, are established (Cabinet of the Ministers, 2014a).

Regulation No. 829 of the Cabinet of Ministers from 23 December 2014 “Special Environmental Requirements for Performance of Polluting Activities in Animal Housing” prescribes environmental requirements for manure management in animal housing. Compared to the old regulations, it sets out requirements for the animal housing unit in particularly sensitive areas and clarifies the requirements for manure storage outside the animal housing (Cabinet of the Ministers, 2014b).

5 Policy progress against Country Specific Recommendations (CSRs) issued 2013

The EU Commission provides Country Specific Recommendations (CSRs) for each MS for consideration and endorsement by the European Council. The recommendations are designed to address the major challenges in relation to the targets of the EU 2020 Strategy. In the following table, the CSRs relevant for climate change and energy are listed, and their progress towards their implementation is assessed.

Existing CSRs	Progress
Pursue efforts to further reduce the tax burden on low income earners in the context of a shift towards more environmental taxes	A new tax on subsidised electricity was introduced – the revenues of which support low income households. However, it increases the cost of renewable electricity generation, with possible adverse impacts to its further development. The Natural Resources Tax rate has been increased and new tax objectsfor example the use of water resources for production of electricity in a hydroelectric power plants (<2 MW), have been introduced. There has also been an increase in the excise duty for petroleum gas and natural gas used for industrial production. And there is a new tax for the use of the motorway by transport vehicles, which are only intended for the carriage of goods by

	road.
Accelerate the development of gas and electricity interconnections to neighbouring Member States to diversify energy sources and promote competition through improved integration of the Baltic energy markets.	167 million EUR co-financing was granted by the EU for the "Kurzeme Ring" third interconnection and the third Latvian-Estonian transmission network interconnection project, both expected to be operational by 2020. First round of modernisation and reconstruction of the Inčukalns underground gas storage facility with overall budget of 89 million EUR is planned to be implemented by 2018.
Pursue efforts to further increase energy efficiency in transport, buildings and heating systems	Transport: Aiming to support electric vehicles and the charging infrastructure in Latvia, a new call for applications under the subsidy programme "Climate Change Financial Instrument" was introduced, with an overall budget of 5 million EUR. Buildings: Draft Law on Energy Efficiency (Energoefektivitātes likums) was developed in 2014. Among others, the law foreseens creation of a national energy efficiency fund. Heating Systems: In 2014 the sixth round of the subsidy programme "Increase of the efficiency of district heating systems" with overall available budget 14,196,678.02 EUR was opened for new submissions.

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