



## Citizens Advice Scotland's Response:

### **CMA: Heat Networks Market Study Update Paper 31<sup>st</sup> May 2018**

The Consumer Futures Unit (CFU), part of Citizens Advice Scotland, uses research and evidence to put consumers at the heart of policy and regulation in the energy, post and water sectors in Scotland. We work with government, regulators and business to put consumers first, designing policy and practice around their needs and aspirations.

We welcome the CMA's headline provisional recommendation that heat networks should be regulated – which is the key ask from our '*Different Rules for Different Fuels*' research last year.<sup>1</sup> As we highlighted, district heating consumers do not have the same protections afforded to consumers of gas and electricity, and regulation is crucial to build trust in the sector as it grows in line with Scottish and UK targets. Although the CMA does not consider options to address monopoly supply such as mandatory re-tendering proportionate, the monopolistic nature of heat networks means particularly rigorous consumer protections are required. The CMA's consumer research and in-depth investigation are welcome and we would like to work closely with the CMA following the conclusion of its market study as recommendations relevant to heat consumers in Scotland are implemented.

#### **1. Do you have views on our approach to analysis and our findings regarding heat network outcomes, misaligned incentives in the supply chain and transparency?**

The CMA's Kantar market research showed how strongly negative experiences can undermine trust and confidence in heat networks.<sup>2</sup> For example, those with negative experiences said they would avoid properties on heat networks, and would caution family and friends against purchasing properties on a heat network.<sup>3</sup> As with any unfamiliar technology, consumer buy-in is crucial if ambitious targets for the growth of heat networks are to be met, so to avoid detriment and reputational damage, a robust consumer protection framework must be in place.

The CFU broadly supports the themes the CMA has focussed on - outcomes for heat network customers, misaligned incentives and transparency. In particular we welcome the specific consideration of protections such as a priority service register, support for vulnerable customers, complaints handling, access to the ombudsman, improved billing, protection from back billing, price setting criteria, contractual protection, and technical standards - all of which our research called for.<sup>4</sup> We would encourage the CMA to give fuller consideration to a number of other consumer protections, namely: support for consumers in

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<sup>1</sup> Consumer Futures Unit, *Different Rules for Different Fuels*, [link](#).

<sup>2</sup> Kantar, *Qualitative Research: Heat Networks*, [link](#).

<sup>3</sup> Kantar, *Qualitative Research: Heat Networks*, [link](#), p.3.

<sup>4</sup> Consumer Futures Unit, *Different Rules for Different Fuels*, [link](#), pp.15-17.



debt, for example through payment plans as offered by electricity and gas suppliers; clear, responsive complaints procedures to seek redress; and compensation for interrupted supply.

## **2. Do you consider the individual household gas boiler price to be a reasonable benchmark for customers to be confident that their heat supply is value for money?**

Meeting a gas benchmark is not a guarantee of affordability as 23% of those who rely on gas as their primary heating fuel are in fuel poverty.<sup>5</sup> Nevertheless, gas prices are less volatile than, for example heating oil, and fuel poverty rates for gas-users are below the national average in Scotland.<sup>6</sup> The fact that communal boiler servicing costs are included in a heat network's costs, unlike an individual boiler where such costs are borne separately, should be itemised in any benchmarking system. The Heat Trust's Heat Cost Calculator currently allows those who know their annual heat bill to compare district heating and modern gas boiler costs, which we believe is a useful model.<sup>7</sup> However, any gas benchmark should be kept under review, and should be in line with the cheapest widely available alternative to district or communal heating to ensure the best outcomes for consumers.

## **3. Have we accurately captured the two broad categories of delivery models in the heat networks market (described in section 5) employed by housing associations and private property developers and their impact on customer outcomes? Do you have any views on potential different categories?**

Property law is different in Scotland compared to England, with no distinction between freehold and leasehold. The Scottish Futures Trust's Guidance Heat Supply Agreements usefully sets out the main delivery models employed in Scotland.<sup>8</sup> It suggests 4 categories: self generation/self supply; self generation/supply to third parties; third party generation/self supply; and third party generation/third party supply.<sup>9</sup>

Section 5 of the CMA's update report focused on privately-operated heat networks as 'the risk of detriment is substantially reduced' on heat networks operated by local authorities.<sup>10</sup> Nevertheless, detriment is still possible on local authority heat networks. For example, the overall cost of district heating can be under-reported due to local authorities absorbing maintenance costs, making potentially inefficient schemes seem more viable.<sup>11</sup> Furthermore, in Citizens Advice's 2016 information request to local authorities in England, Wales and Scotland, it was found that only 38% of schemes shared with customers how

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<sup>5</sup> *Scottish House Condition Survey: 2016*, [link](#), Table 34.

<sup>6</sup> BEIS Fuel Price Indices and a Weighted Average for Scotland, cited in *Scottish House Condition Survey: Key Findings*, [link](#), p. 66.

<sup>7</sup> Heat Trust Cost Calculator, [link](#).

<sup>8</sup> Scottish Futures Trust, *Guidance on the development of Heat Supply Agreements for District Heating Schemes*, February 2018, [link](#)

<sup>9</sup> Scottish Futures Trust, *Guidance*, [link](#), pp.7-8

<sup>10</sup> CMA, *Update Paper*, [link](#), p.58.

<sup>11</sup> Which? *Turning Up the Heat*, [link](#), p.18.

their bill was calculated, reinforcing the need for stronger consistent requirements to ensure billing transparency.<sup>12</sup>

**4. Do you have views whether heat networks should be regulated? If you agree that they should be, please provide any views on which body might be best placed to act as the sector regulator.**

Yes, we consider heat networks should be regulated. Consumer protections for heat network users are not codified in one place, leaving gaps in protection, particularly around debt protection, access to the Ombudsman, registering on a Priority Services Register, guidance for vulnerable consumers, and providing energy efficiency information. Our *Different Rules for Different Fuels* research indicated wide support for regulation from both suppliers and other stakeholders, and an acknowledgement of the need to improve consumer protections.<sup>13</sup> It also indicated that a regulator could be responsible for: issuing licenses and assessing the compliance of suppliers with license conditions; keeping a register of schemes; taking appropriate enforcement action where appropriate; requiring and supporting suppliers to provide advice to consumers on how to use heating systems; providing access to the Energy Ombudsman.

Our legal opinion found that responsibility for the regulation of district heating is devolved to the Scottish Parliament, although legislation around consumer protection is reserved to the UK Government. The Scottish Government therefore does not have the power to legislate for any new consumer protections, but has proposed to codify protections that exist in UK and EU law under guidance alongside a licence, as we called for last year.

Given this spread of responsibility across devolution boundaries, and the CMA's desire for consistency of protection across the UK, we support its intention to continue to engage with the Scottish Government about how best to protect Scottish consumers. It may be that a solution would be to establish a UK framework that would then enable the Scottish Government to include comprehensive consumer protection measures within a licensing scheme.<sup>14</sup>

**5. If there is sector regulation, should it apply to all communal and district heating networks, all delivery models and existing as well as new networks?**

We recognise concerns that regulation appropriate for larger suppliers may be disproportionate for stand-alone providers of very small schemes. While we do not consider that service standards for consumers should be relaxed in these cases, we recommend additional, targeted support for small suppliers where necessary to enable them to meet required standards.<sup>15</sup> It is important that heat network consumers on smaller schemes do not face the prospect of the costs of higher compliance being passed on, so models such as

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<sup>12</sup> Citizens Advice, *District Heating Networks: Analysis of Information Request*, January 2016, [link](#), p.10.

<sup>13</sup> Consumer Futures Unit, *Different Rules for Different Fuels*, [link](#), p.3.

<sup>14</sup> Consumer Futures Unit, *Different Rules for Different Fuels*, [link](#).

<sup>15</sup> Consumer Futures Unit, *Different Rules for Different Fuels*, [link](#), p.14.

joint procurement or combined vulnerability strategies should be explored. Those on smaller rural schemes may experience distinct types of detriment which regulation should address, such as high costs or a lack of customer consultation prior to decisions. For example, a case from one of our Citizens Advice Bureaux showed a farmer installing a scheme having had little consultation with his tenants at a cost of £150 per month for hot water.<sup>16</sup>

**6. Do you have views on whether regulation of heat network prices to end customers is appropriate? If there were a form of price regulation, should it be a cap at a certain level, or a 'principles based' approach with self-reporting against permissible contract terms and a regulator to investigate complaints? What factors should determine the maximum level of prices?**

Our research identified 3 possible consumer protections around pricing: benchmarking, the publishing of prices; and price capping.<sup>17</sup> Given recent moves to set a price cap for gas and electricity in a competitive market, and considering the monopolistic nature of heat networks, we consider there to be a strong case for a cap on prices for end heat consumers. However, as noted in the CMA's update paper, it is important that a cap is not seen as a target which suppliers raise their prices to meet, as has occurred in the Netherlands, so a thorough analysis of the potential impact of a cap would be necessary first.<sup>18</sup>

If a cap is adopted, price setting criteria and monitoring must be robust. The process for setting a cap would be complicated by the fact that the size and nature of schemes can vary significantly, and the potential savings to the consumer will depend on what, if any alternative fuels are available. There is, for example, a significant difference between gas and electric heating. One option would be to set prices at a level that is no more than the equivalent cost of the cheapest alternative heating system.

The CMA rightly emphasises the importance of transparency and the publishing of prices is one way to achieve this. We have not conducted research on the viability of the CMA's principles based proposal, but note Ofgem's move towards a principles based approach in the regulated energy markets. While we cannot be certain of the consumer impacts of such an approach at this stage, it will be important to monitor developments closely and ensure appropriate resourcing to ensure the highest standards for consumers. Overall, providing that monitoring and price setting criteria are robust, a principles based approach could provide the flexibility needed to regulate a varied heat network market.

**7. Do you consider that any rules and guidance on pricing and quality should apply to all heat networks or, for example, only to those with ESCOs? Do you consider that it would be proportionate to ban 'capital contributions'?**

We do not take a view on banning capital contributions from property developers to ESCOs. However, our concern is the impact on the consumer, so any model that disproportionately increases costs for consumers should be discouraged. Regarding pricing and quality, we believe that regardless of who manages a heat network, consistent, effective protections

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<sup>16</sup> Confidential CAB data.

<sup>17</sup> Consumer Futures Unit, *Different Rules for Different Fuels*, [link](#), p.10.

<sup>18</sup> CMA, *Update Paper*, [link](#), p.25.

should be in place for all consumers, and set out possible approaches to pricing are set out in the previous question.

**8. Do you have views on whether heat network customers should have similar consumer protections to customers of regulated gas and electricity utilities?**

Yes, we believe heat network consumers should have as a minimum the same protections afforded to those who use gas or electricity. However, with around 14,000 heat networks around the UK, compared to 69 gas and electricity suppliers, the distinct experiences of gas, electricity, and heat network consumers must also be acknowledged.<sup>19</sup> A number of enhanced consumer protections may therefore be required for heat networks, especially given the inability to switch supplier and the possibility of longer delays if supply is interrupted. These could include price capping, benchmarking, or the publishing of prices, as set out in our response to question 6.

**9. Do you have views on the recommendations described in section 7 that we are minded not to pursue (eg banning capital contributions from ESCOs to property developers, and mandatory re-tendering of heat network operating and billing contracts)?**

We do not take a view on this.

**10. Do you have views on how to improve technical standards, which cover the design and operation of heat networks, and make them enforceable? Could this be achieved in the absence of a regulatory regime requiring a licence to operate a heat network? For example:**

If the main two aims of heat networks – to reduce costs and carbon emissions are to be achieved robust technical standards are critical. Inefficient schemes actively undermine these goals, reduce trust in heat network technology, and can lead to inflated prices for consumers. Our research indicated that minimum and maximum temperatures, pressure controls, and annual reporting on the efficiency of schemes, are some technical standards that could improve outcomes for consumers.<sup>20</sup> We welcome that the Scottish Government is taking forward our proposal to licence heat networks and believe a licensing scheme is best reinforced by overarching regulation.

- a. What is the role of the CIBSE ADE CP1 Code of Practice in this process?

Regulation of technical standards should build on the Heat Network Code of Practice Scheme developed by the Association for Decentralised Energy and CIBSE, although further work may be needed to determine how this could be applied to existing schemes.<sup>21</sup>

- b. Do you have views on how these proposals could be embedded in the planning authorisation process?

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<sup>19</sup> BEIS, *Experimental Statistics on Heat Networks*, [link](#); Ofgem, *Number of Active Suppliers*, [link](#).

<sup>20</sup> Consumer Futures Unit, *Different Rules for Different Fuels*, [link, p.16](#).

<sup>21</sup> CIBSE/ADE Code of Practice, [link](#).

We do not take a view on this.

c. For potential heat network connections affected by Building Regulations and / or planning, how could appropriate technical standards could be embedded these processes at local, regional and national levels?

We do not take a view on this

d. Could operating technical standards be applied retrospectively to existing heat networks?

We don't take a view on this

e. What is the impact of the current approach to professional indemnity insurance for heat network design and build on the recommendations of design engineers?

We do not take a view on this.

**11. How could local and development plans and their supplementary guidance be adjusted to take lifetime costs and customer prices into account? What would the impact of this be?**

Under the Scottish Government's proposals for Local Heat and Energy Efficiency Strategies (LHEES) socio-economic assessments will be required at strategy, project and building level, aimed at addressing fuel poverty. In our response to the Scottish Government's consultation, we noted that areas with high rates of fuel poverty are often not the most profitable for developers, so it is critical that these assessments have a practical use and effectively target those in fuel poverty.<sup>22</sup> We also noted the overall need for LHEES to align and co-ordinate with existing local government plans, such as Local Development Plans.<sup>23</sup> Therefore the introduction of district heat regulation would need to closely complement LHEES in Scotland, especially in areas where local authorities are likely to be district heating providers.

**12. How should a heat network quality assurance scheme be established and embedded into the regulation of heat networks? Should such a scheme seek to accredit the commercial, financial and contractual aspects of a heat network as well as the technical?**

Any quality assurance scheme should take a holistic approach to the various aspects of a heat network, whether commercial, financial, contractual, or technical. We note the Scottish Government's proposal that a licence would ensure technical and operational standards, and network compatibility, and this is a model that the CMA could explore. Our view on minimum technical standards is set out in response to question 10 (a).

We also recommend that the CMA consult the Each Home Counts Board which is currently drawing up a UK-wide Quality Assurance framework for installers of energy efficiency and

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<sup>22</sup> CFU Response to the Scottish Government's Second Consultation on Local Heat & Energy Efficiency Strategies, and Regulation of District and Communal Heating, [link](#).

<sup>23</sup> Ibid.



renewables measures. There may be some useful insights to draw from this and apply to heat networks.

**13. Is further information required to improve consumer understanding of the significance of living in a home with a heat network? If so, what information would be useful?**

Yes, information is one of the Consumer Futures Unit's guiding principles and we support the CMA's objective of improving transparency around heat networks.<sup>24</sup> Kantar's research commissioned by the CMA showed that some consumers only gain a full understanding of their heating system after they have moved into a property and sometimes only once supply has been interrupted.<sup>25</sup> Kantar identified an underlying assumption from consumers that utilities operate in the same way, so the inability to switch supplier can be a particular surprise to those on heat networks.<sup>26</sup> Our *Hot Off the Grid* report research found that consumers may require additional information on how to use newly installed heating systems beyond initial written or verbal instruction. This is particularly important regarding heat networks, where knowledge and experience of the system can be more limited. The research recommended that support to tenants include: demonstrations and in-home explanations on how to use the system; easy-to-understand and simple written instructions; follow-up advice; greater support for vulnerable tenants e.g. elderly tenants; advice for new tenants when moving into the home, as well as when new systems are fitted; and advice on the most appropriate tariff (and in some cases advocacy to resolve disputes with energy suppliers).<sup>27</sup>

**14. Who should be responsible for ensuring that new leasehold agreements include a clear reference to the treatment of heat network assets connected to a leasehold property?**

We do not take a view on this.

**15. Should heat supply agreements or contracts which set out key performance indicators, such as guaranteed terms of service, be made compulsory?**

As the CMA noted, there appears to be a low incidence of heat supply contracts, meaning key information, contractual rights and obligations may not be available – a concerning situation given the inability of heat network consumer to switch supplier.<sup>28</sup> Our research recommended that Fair Heat Contracts should be the norm for heat network consumers, clearly setting out consumer protections, as well as leaving and joining rights.<sup>29</sup> The regulator should issue guidance and monitor the fairness of such contracts. The CFU supports the CMA's proposal to include key performance indicators such as response times

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<sup>24</sup> Consumer Futures Unit, *Consumer Principles*, [link](#).

<sup>25</sup> Kantar, *Qualitative Research: Heat Networks*, [link](#).

<sup>26</sup> Kantar, *Qualitative Research: Heat Networks*, [link](#).

<sup>27</sup> Consumer Futures Unit, *Hot Off the Grid*, [link](#), p. 73.

<sup>28</sup> CMA, *Update Paper*, [link](#), p. 75.

<sup>29</sup> Consumer Futures Unit, *Different Rules for Different Fuels*, [link](#), p.10.

to outages, complaints handling, dispute resolution arrangements and annual cost estimates.

## **16. How could EPCs be improved in relation to heat networks?**

As noted in Heat Trust's annual report EPCs do not include repair and maintenance costs associated with heating a property, whereas heat bills generally do, leading to some confusion when costs are higher than expected.<sup>30</sup> We echo Heat Trust's recommendation that EPCs for properties on heat networks should at the very least clarify that standing charges detailed in final bills may include additional repair and maintenance costs. In our response to the Scottish Government's first district heating consultation, we also raised concerns that the EPC register needs to more accurately reflect 'real time' demand, rather than relying on current modelling, in order to avoid inefficiencies such as over-capacity when designing schemes.<sup>31</sup> Following concerns that EPCs in general do not reflect household consumption, the Scottish Government is reviewing EPCs, and we welcome its stated desire to use this to improve the provision of information to heat network consumers.<sup>32</sup>

## **17. Should heat supply bills be improved? Is further information necessary? If so, what information would be helpful?**

Our research indicated that bills can be confusing for consumers with particular issues around back-billing. One consumer believed that their heating was paid with their rent and only realised this was not the case once £300 of debt had accumulated.<sup>33</sup> The CFU recommends a clearer percentage breakdown of contributing components of the bill, including maintenance charges. This would give the consumer the opportunity to see what contributes to cost, and what savings could be available by reducing use. The fact that billing was most common complaint referred to the Ombudsman by the Heat Trust, highlighted ongoing issues with the clarity of billing, especially around standing charges. Furthermore, prepayment meters appear to be a factor in making it harder to understand costs, including unit price, whether tariffs include standing charges, where to get information and how charges are broken down.<sup>34</sup>

## **18. Should there be specific requirements regarding the frequency of bills beyond that already required by the Heat Network (Metering and Billing) Regulations?**

Yes, bills for those on heat networks should be as regular as those provided to consumers of gas and electricity. Under the Electricity and Gas (Billing) Regulations 2014, suppliers must make available a bill at least twice a year or at least quarterly to any consumer who requests it or has an online account.<sup>35</sup> The Heat Network (Metering and Billing) Regulations

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<sup>30</sup> Heat Trust, *Annual Report*, [link](#).

<sup>31</sup> CFU Response to the Scottish Government's Second Consultation on Local Heat & Energy Efficiency Strategies, and Regulation of District and Communal Heating, [link](#).

<sup>32</sup> Scottish Government's Second Consultation on Local Heat & Energy Efficiency Strategies, and Regulation of District and Communal Heating, [link](#).

<sup>33</sup> Consumer Futures Unit, *Different Rules for Different Fuels*, [link](#).

<sup>34</sup> Consumer Futures Unit, *Different Rules for Different Fuels*, [link](#), p.21.

<sup>35</sup> Electricity and Gas (Billing) Regulations 2014, [link](#).



2014 state that bills must be issued once a year, but this is only provided that the customer or supplier has taken a meter reading, and as recent figures from BEIS indicated, 60% of heat network consumers in Scotland are unmetered.<sup>36</sup> Ofgem has recently banned suppliers from backbilling gas and electricity customers beyond 12 months, and it would be consistent to apply the same principle to heat networks.<sup>37</sup>

**19. Should standard performance metrics for suppliers be produced – for example, in relation to planned and unplanned outages and heat temperatures? Should this information be published?**

BEIS' research in England and Wales indicated that heat network consumers are more likely to experience over-heating than those not on heat networks, and this can lead to energy inefficient behaviour, such as the opening of windows or use of electric fans.<sup>38</sup> As set out in response to question 10 (a), technical standards could be a way to address these problems such as through minimum and maximum temperatures, pressure controls, and annual reporting on the efficiency of schemes.

Vulnerable consumers are most likely to be effected by outages whether planned or unplanned, and our research recommended a minimum level of service regarding fault handling and repairs, including response time and ensuring continuity of supply. The CMA's report did not address the issue of compensation for outages which we believe should be in place to incentivise suppliers to reduce the number and extent of breakdowns, and bring district heating suppliers in line with other energy companies. Where service interruptions are scheduled, advance notice should be provided as the norm. Additional support, such as the provision of alternative heating in emergencies, should also be targeted at vulnerable consumers through a Priority Services Register.

**Marcus Wilson, Energy Policy Officer**

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<sup>36</sup> Heat Network (Metering and Billing) Regulations 2014 , [link](#); BEIS, *Experimental Statistics on Heat Networks*, [link](#).

<sup>37</sup> Ofgem, [link](#).

<sup>38</sup> BEIS, *Heat Network Consumer Survey*, [link](#), p.3.