

Competition and Markets Authority
Victoria House
37 Southampton Row
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CMA's Market Study Consultation

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?

Date 31 May 2018

We note that the WLC of heat networks does not benefit at present from the disaggregation of the value chain to clearly separate generators, suppliers and distributors. Arguably, such conditions would stimulate competition, drive innovation and enable costs reductions, and these were indeed design criteria for the liberalisation of the electricity market.

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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 placed to act as the sector regulator.

We agree with the CMA in relation to the benefits that a regulator could bring to the market and we do consider a cost-plus pricing policy could be appropriate.

We believe that a cost-plus pricing policy would only be effective if transparency between the district heating company and the regulator, and between the district heating company and the consumer, could be realistically put in place.

In **Denmark**, fair price is ensured through the following **model**:

- Prices can include all the necessary costs, and not more!
- The utility calculates and announces prices to the regulator
- The regulator notifies the tariff and announce statistics

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- The consumers can complain to the regulator
- The regulator can declare that tariffs shall be changed
- The tariff can include depreciation of planned investments 20% per year in advance
- The typical DH tariff:
 - A fixed component per m² floor, per kW or per 3-year MWh
 - Discount on the fixed component to large consumers
 - A variable component (will be time dependent, e.g. monthly)
 - An incentive to reduce the return temperature

We think that since **OfGem** regulate other energy markets, it would be sensible that they do the same for the heat market, especially since it is likely to have same or similar value chain and with the synergy benefits from whole system approaches.

Finally, whilst we agree on the benefits that a regulator could bring to the market, we question whether a fundamental variation on the delivery model of heat networks should be advocated in the first place.

A more efficient model could potentially promote the **disaggregation of the value chain** to create a net separation between generators and the network operator, in the short terms, and among generators, suppliers and network operators in the long term when an extensive infrastructure will have potentially been developed.

In this model heat networks would be planned with a long-term vision, accounting for future extensions and interconnections, as well as for potential locations of new generating plants. The network operator would install and maintain the network and would tender for generators to connect on a £/MWh basis.

Moreover, this model would in principle reallocate risks to various parties and could reduce the weighted average costs of capital to develop heat networks.

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

In our view **CP1 has contributed to set and raise standards** in the industry. Even though it is not mandatory, in our experience this is generally a client's requirement, particularly when this comes from the public sector. Moreover, compliance with CP1 is in such cases assessed thoroughly.

Ramboll believes that CP1 should, in fact, be made more comprehensive to cover existing gaps and should be made **mandatory**.

