

Heat networks regulation: fair pricing protections consultation response

ASTER
GROUP

Introduction

While we have considered and responded to all applicable questions, our overarching belief is that a different, less onerous approach should be taken for not-for-profit social housing providers on fair pricing regulations. As the Government will be aware, our sector has challenges when it comes to meeting the various requirements due to the complexities brought about by the number of heat networks owned by us, the age of our stock and the types of homes we own and manage.

Implementing these regulations would impose significant costs on our sector with limited financial support. It will also add an administrative burden to an already highly regulated sector, and cost which we would not want to be passed onto the most financially vulnerable in our society. Requirements must therefore be proportionate.

Consumers are likely to face increased prices due to the need for greater cost recovery associated with transparency and higher administrative demands. We do not believe therefore that introducing these regulations will achieve the desired outcomes.

The purpose of the new heat network regulations is partly to encourage greater investment and help to decarbonise the grid. We contend that these fair pricing requirements may disincentivise investment and installation in new homes.

Question 1. Have we identified the right set of fair pricing consumer objective, principles and outcomes and are these properly defined? If you disagree with this proposal, please specify what changes you would like to see and provide a justification.

While we agree at a high level with the set of objectives, principles and outcomes chosen, and understand that the overall application of a fairness test in the regulatory regime should ensure a balanced approach is taken, we are concerned that, unless the expectations on authorised parties regarding the principles are explicitly and unambiguously stated, these could change. Taking cost efficiency as an example, as a not-for-profit social housing provider, we have a large amount of ageing stock with older systems; more than 40% of our heat networks are over 30 years old. These could be practically hard to replace without disruption to customers, and financially difficult without external support. An expectation to implement technical efficiencies at these complex sites and have the financial resources to do so would have a negative effect on customers and drain much-needed resources. We would therefore welcome further clarity on Ofgem's expectations, particularly for not-for-profit providers, and additional financial support to deliver necessary upgrades.

Question 2. Do you agree with our proposals to develop the fair pricing guidance in relation to the principles? In particular:

- a. Have we identified the right areas to be covered by the guidance implementing the fair pricing principles?**
- b. Do you agree with the specific proposals to develop each of these areas in guidance?**

We welcome additional guidance in all the areas mentioned as this will help us to understand practically what is expected of us as a heat network operator. However, recognising the unique position of social housing landlords as heat network operators, we would also welcome guidance on how these rules intersect with the existing Social Housing Regulations and other common practice in the sector.

For example, capital cost recovery for major works for leaseholders would traditionally involve a Section 20 consultation process, but whether this process continues to exist, and whether we are able to build up a sinking fund over time to spread the cost for leaseholders, is unclear. Similarly, if we are required to unbundle all heat supply and maintenance charges from existing rents and service charges, this will require a variation to the lease. This typically involves a First-tier Tribunal under the Landlord and Tenant Act 1987, which will come at a cost to us.

We would welcome guidance on what process to follow, given the number of customers that will be affected by these changes, and a commitment of additional funding to support with this to keep costs as low as possible for the business and our customers. It is worth highlighting at this point that, while we agree with the fairness of individual metering, additional costs for third-party metering and billing agents where we do not have the resource in house may also increase costs.

Equally, there are some areas of guidance that we feel do not reflect the underlying business aims of social housing providers and not for profits. As a not-for-profit housing association, our only requirement is to recover our costs, with any surplus directed back into serving customers. If costs are not recovered, this can impact the service we deliver to all our customers. We also have an existing obligation under both the Procurement Act and the rules set out by the Regulator of Social Housing (RSH) to deliver value for money to our customers. With this in mind, much of this guidance around cost efficiency, fair and reasonable returns, and affordability does not reflect the nature of our business and feels excessive given the regulation we are already subject to. Additionally, without extra funding, upgrading some of our older networks will be impossible, but we are concerned that this guidance suggests this could attract regulatory intervention. We would therefore welcome additional funding to support these aspirations.

Question 3. Do you agree with the proposed 'fairness test'? In particular:

- a. Do you agree with the high-level features of the fairness test?**

We agree with the general approach to assess fair pricing in a way that is reasonable and done on a case-by-case basis, owing to the crossover in regulation for social housing providers, the existing strong regulatory control for social housing providers, and the lack of resources to carry out upgrades which might improve efficiency.

b. Do you agree with our proposals to implement the fairness test discussed in Appendix 1: Fairness test?

With regard to the specific points in Appendix 1, we have two concerns we wish to highlight.

Firstly, while we appreciate the intent of benchmarking against alternative technologies and understand that this is one small component of the fairness test, the Heat Trust itself caveats that its gas heating benchmarking tool is not intended to show whether the prices paid by heat network consumers are fair.

There is far too much variation within the existing heat networks, due to age, model, building type and maintenance history, to consider this benchmark a test of fairness of pricing, and we therefore do not believe it should be included.

Secondly, although we understand that the individual circumstances and vulnerability of a customer impacts how much disproportionate pricing might affect them, we do not believe that any organisation should be treated differently under fair pricing investigations because of the makeup of their customer base. Social landlords inherently serve a greater proportion of vulnerable customers, and we would not wish to see social landlords receive greater investigatory attention or a higher risk of penalisation because of this.

Furthermore, as a not-for-profit organisation, there is no profit motive to drive the behaviours that may result in unfair pricing. Historically we have inadvertently subsidised heating provision, and the new methodologies needed to provide the transparency required under the regulations will in all likelihood increase costs to the residents.

Finally, the purchasing of fuel under commercial arrangements won't always achieve the discounts domestic customers receive, so the publishing of data in this regard may result in complaints of unfair pricing where this does not exist.

Question 5. In relation to market segmentation:

a. Have we identified the right characteristics for market segmentation, and are these correctly defined?

We see the benefit of collecting data on all these criteria and support the concept of segmentation for the purposes of better understanding the market and adjusting enforcement as appropriate. However, to use all of these characteristics to segment the market for comparison is, in our view, too complex. The challenge of segmenting such a diverse market is significant; even within not-for-profit social landlords, there are different stock profiles, business models and ways of recovering costs which would make price comparisons very difficult. We appreciate the breadth of characteristics considered here but remain concerned that the market is simply too diverse to account for all differences and draw meaningful comparisons.

b. Do you agree with the segmentation approach discussed for each of these characteristics?

We strongly support different approaches based on for-profit/not-for-profit status, and for different housing tenures, and particularly welcome further exploration of how price regulation and housing legislation interact. It is worth noting that not all social landlords are run on a not-for-profit basis, and we would expect a different approach for these segments. We echo The Heat Network's call in their response for a clear definition of not-for-profit.

Question 6. Of the information listed in Table 3, what do heat networks already regularly collect and can be easily reported?

Question 7. Of the information listed in Table 3, which items would be more challenging for heat networks to report?

Question 8. Of the cost drivers listed in Table 7, which items would be more challenging for heat networks to report?

Question 9. Should certain types of heat networks have more limited data reporting requirements? If so, which heat networks should these reduced requirements apply to, and what data should they be exempt from reporting?

We agree with the response from The Heat Network (THN) that we would be able to report on most of these items. However, for networks that are currently unmetered, annual network demand and some of the charges data may be difficult to provide. We acknowledge that metering may be required in future under HNTAS which will help to meet this standard, but stress that the cost and disruption for residents, particularly in older buildings, will be significant.

Additionally, some technical information such as flow temperature and other efficiency measures may be hard to obtain, especially for older networks and buildings that have come into our ownership through stock transfers. Network length is not commonly known and would be impossible to determine without costly surveys.

Reduced reporting should therefore be in place, and as stated at the start of this response, we do not believe that not-for-profit social landlords should be subject to much of these requirements. Where reporting requirements do apply, we would welcome more thorough definitions of all of these items, to ensure data is consistent and correct.

We would also stress that, while we would technically be able to report on most of these items, ensuring that the underlying data is structured and formatted so that it can be easily accessed, regularly and accurately reported, and done in as automated a way as possible to reduce administrative burden, is in itself a process that will take time and resource. As THN note in their response, there is also some overlap between this and the HNTAS requirements. We would welcome reporting processes that are as streamlined as possible across the regulations, as well as time to develop and implement processes internally. We would be happy to share further information about how our data is structured and the work that needs to be done to automate this reporting if it would be helpful in developing guidance and best practice.

Question 10. Do you agree with our proposed prescriptive rule that GSOP payments, compensations, fines, penalties and other redress provided to consumers should not be passed through to customers?

We agree that customers should be protected from effectively subsidising financial penalties for poor performance. Therefore, we do not believe that fines are the correct way to enforce regulation for not-for-profits, as this would take vital money out of the business, leaving the poorest and most vulnerable in the country effectively covering these costs. Our social purpose means we will always endeavour to meet high standards of performance for our customers. However, where things do go wrong, we believe the best course of action would be a process aligned with that of the RSH, i.e. a regulatory downgrade and an action plan to improve standards. As stated in our response to the latest consumer protection consultation, we support paying compensation to heat network customers as we do for all other customers, and do not directly pass these costs on. However, to make this process sustainable and fair across our customer base, we would welcome the ability to retain control of these rates and the award of compensation. We must reinforce that, owing to our not-for-profit model, in not passing on the cost to the heat network customers, these costs would disadvantage residents who do not receive the benefit of the heat network, and may live in fuel poverty already.

Question 11. Do you agree with the draft best practice guidance provided? Is there anything that should be added? Should any of the best practice guidance be strengthened to prescriptive rules?


We agree with the draft best practice guidance provided, and do not believe there is a need to strengthen this to prescriptive rules, particularly for not-for-profit social landlords, for the same reasons as previously discussed. We would welcome clarity however on whether there is an expectation that we demonstrate our calculations for efficiency losses and if there is a prescriptive way of doing this.

Question 12. Do you think that the best practice approach to cost allocation should differ for different types of heat networks, or different types of suppliers? If so, for which types and how?

As previously stated, we believe that heat network operators whose entire business is run on a not-for-profit model (i.e. not just the heat network services), and particularly social landlords, should not be subject to extraneous regulation or administrative burden. Our business operations are underpinned by our social purpose, and there are therefore no drivers for us to inflate prices for customers beyond what is necessary to cover our costs.

Question 14. What other feedback do you have on the proposed approach to cost allocation?

In order to comply with the fuel procurement part of this guidance, we would welcome access to less commercially constrained fuel costs. We currently purchase our fuel on commercial, not



domestic rates, which could have a major impact on the price for customers. We would welcome consideration of whether registered providers of social housing could be granted access to the government fuel purchasing framework, as Local Authorities are able to do, or if a new procurement framework could be set up. This would ensure fair pricing for all social housing tenants, regardless of whether their landlord is a Local Authority or a Housing Association.

Question 15. Do you agree with our proposed approach for defining heat network prices in a comparable way? Are there any other ways to define price that we should consider?

We welcome that fixed pricing structures will not be introduced, due to the variety in heat network providers. However, we recognise the difficulties with both methods of defining heat prices. On the one hand, different pricing structures and different types, tenures and needs categories of residents could skew a price per year per customer figure. On the other hand, defining high and low usage consumers would be difficult without contextualisation from customer data, and collecting information from residents about their personal circumstances would not be proportionate to the outcomes. In addition, in older buildings it is often the case that residents don't have individual control of heat.

Implementing comparable pricing definitions for existing heat networks in old buildings will be incredibly difficult. Going forward, we can understand the need to build in metering and thermostats so residents have control, and prices can be better compared, but we highlight again the cost, complexity and disruption associated with applying these regulations on old systems.

Question 16. Do you agree with our proposal to use gas boilers and heat pumps as external reference benchmarks?

No, as we do not believe that these are able to provide meaningful comparisons.

Question 17. Do you agree with the proposed method for calculating a heat pump benchmark, including the key input parameters outlined? Are there any additional factors that should be considered to ensure a robust heat pump benchmark?

We understand the rationale behind providing customers with both a current and future-proofed counterfactual. However as previously discussed, we feel there is simply too much variation in age and model of boilers and heat pumps, as well as differences in property type, presence of cladding and tenure of occupants for these to provide a meaningful comparison. We accept that this comparison may be better suited to new systems than old ones.

Question 18. Do you agree with the proposed approach to comparator benchmarking, and our list of potential cost drivers set out below and in Appendix 3: Cost driver? Are there any relevant cost drivers that we haven't considered?

If the comparable price is taken as the charge per customer per year, we believe tenure of property could be a cost driver, as the needs of residents can have a big impact on energy used. Most of our heat networks are in extra care schemes, the residents of which often have higher heating requirements.

Additionally, we believe the age of the system should be a high importance cost driver, as this has a major effect on efficiency.

As previously mentioned, network length is widely unknown and would require costly surveys to determine.

We appreciate that the list of cost drivers is long and the model complex because we are trying to map a complex system. But we have concerns that this process is overcomplicated and unnecessarily burdensome.

Question 19. What is your view on the ease with which data could be reported on the four 'High Importance' cost drivers set out in paragraph 4.33? What information do heat network operators and suppliers already collect, and what would be challenging to provide?

Question 20. What is your view on the ease with which data could be reported on the remaining 'Medium Importance' cost drivers set out in paragraph 4.33? What information do heat network operators and suppliers already collect, and what would be challenging to provide?

Question 21. What is your view on our proposal to publish a high-level methodology for each benchmark (once data is collected and methods have been tested), to provide an accessible overview of the approach?

As with the market segmentation reporting, while we could report on all of these cost drivers (with the exception of network length), the difficulty will be implementing the data architecture, systems and business rules to do so with minimal administrative burden and maximum consistency and accuracy. We would also need clear definitions of these cost drivers, flexibility for unmetered networks for which not all information will be available, and a streamlined approach to ensure data is reported once only.

The cost to do this work is of great concern and we would stress that every piece of work we do that requires extra resource has a knock-on impact on all of our customers, not just those on heat networks.

Any guidance that would help consumers understand these figures is welcome, but we would stress the need to communicate to a wide audience and provide for customers with a range of accessibility needs.

Question 22. Do you have any other feedback on the proposed approach to price comparison and benchmarking?

As in our initial remarks in this response, we do not believe that over-burdensome and complex reporting requirements should be applicable to not-for-profit social housing providers.

We do not believe either that these requirements will incentivise investment in heat networks and help to decarbonise the grid, which is part of the purpose of a more regulated heat network sector.

Question 27. What are your views on the three options? Please comment on each option in terms of the price information to be centrally published, how the price information is presented and what prices are compared to.

Question 28. Do you think the options have the right balance between providing a good level of transparency, burden on consumers to interpret the information, risks of misinterpretation by consumers, disclosure of commercially sensitive information, and risk of price convergence?

Question 29. Do you support focusing on one option or a combination of options in paragraph 6.69?


While we understand and support the intention to provide customers with more information and greater transparency, we are concerned that there is a risk of misinterpretation. Although we understand this is not representative of all heat network operators, the majority of our heat networks serve schemes which are designed for people who need additional support. We would want to be sure that any information presented to them was clear, intelligible and accessible, to avoid confusion and distress.

As previously stated, we will only charge customers what is necessary to cover our costs, and therefore there is no risk of price convergence from our perspective.

We echo the response of THN that we are not best placed to answer which option or combination of options provide the most robust methodology, and stress that any solution must be clear for customers and contextualise the differences between not-for-profit and for-profit providers.

Question 30. Do you support the phasing in of the options described in paragraph 6.70?

We have some concerns about clarity for customers if options are phased in and give a different impression of performance over time. But we welcome time to gather data and put in place reporting structures to minimise administrative burden. We strongly stress that much of the new Consumer Protection regulations, including fair pricing, will need to be automated and data driven to ensure compliance and consistency, without excessive manual processes. Major changes to systems, data, and business rules will therefore be required. As a sector, we have had to deal with a raft of new legislation over the past five years, from Building Safety to Tenant Satisfaction Measures. We will always be committed to delivering the very best for customers, and protecting



their best interests, but we welcome the time to implement these changes and make sure we get it right.

Question 31. Do you support the adoption of different options for different heat network groups described in paragraph 6.71?

Yes, we support different requirements for different groups of providers, including not-for-profit social housing providers.

Question 32. Do you agree that central price transparency measures are unlikely to put additional administrative burden on heat networks in addition to data reporting for benchmarking? Do you have concerns on the administrative burden from any options?

Though we acknowledge the similarities in reporting requirements and welcome a streamlined process to ensure reporting efforts are not duplicated, the administrative burden will still be significant, and we have serious concerns over how we would fund and deliver this additional resource.

Question 33. Do you think it is appropriate to link central price transparency with benchmarking?

Yes, insofar as reporting requirements apply to not-for-profit social housing providers.

Question 34. Do you agree with the approach to price investigations set out so far? Please provide reasons and views to support your response.

We welcome an approach that supports and strengthens existing routes of redress, as it is crucial that any new regulation respects and works in harmony with existing housing regulations and practices. We are therefore pleased to hear that more work is being done to understand these interactions, and would encourage as close a working partnership as possible with the RSH so that, where necessary, enforcement action can be taken in a way that is consistent with and supports our working practices, as previously mentioned.

While the overall approach to investigations seems sensible, as we have highlighted throughout this response, we do not believe that not-for-profit housing associations should be subject to extensive data collection and benchmarking requirements, as there is no incentive for us to charge disproportionate prices to customers.