

Heat Networks Regulation: Fair Pricing Protections Consultation Feedback

Fair pricing framework

- 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.**

Would fair pricing split the “cost reflective” aspects into ‘standing charge’ and ‘use’ components? For example, the fuel costs are a ‘use’ cost, and the costs for operation and maintenance of the heat network, and metering and billing costs, are either rolled into one ‘standing charge’ cost on a bill, or separated out on a bill, or should all these components of a bill be presented in a single figure to the resident/customer?

Will there be guidance issued around “cost efficiency”, around how long capital investment costs should be averaged across customer bills, and how the cost of capital works should be deemed as having an acceptable or excessive impact on bills?

Otherwise, all seems right and properly defined.

- 2. Do you agree with our proposals to develop the fair pricing guidance in relation to the principles (please note that questions on cost allocation proposals, including guidance, are asked separately under Chapter 3: Cost allocation). In particular:**
 - a) have we identified the right areas to be covered by the guidance implementing the fair pricing principles (see paragraph 2.53 for a summary of the areas we are proposing to develop in guidance under each principle)? If you disagree with this proposal or think other areas should also be included, please specify what changes you would like to see and provide a justification.**

Would costs of decommissioning a system be included, or would the remainder of a sinking fund be able to go towards this if a heat network were to be removed? Or should the sinking fund be reallocated to residents in a final bill – if so, how should this occur proportionately?

- b) Do you agree with the specific proposals to develop each of these areas in guidance? If you disagree, please specify what changes you would like to see and provide a justification.**

Agree.

- 3. Do you agree with the proposed 'fairness test'? In particular:**
 - a) Do you agree with the high-level features of the fairness test (principle based, reasonableness, case-by-case basis, and objectivity)?**

Yes. I like that objectivity is conditioned by case-by-case and reasonableness and vice versa.

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

How regularly would these questions be asked? Would they be cascaded i.e. the questions in sections "A1.3" "A1.4" would only be asked if there were to be an issue with those in "A1.2"? how would comparisons with alternatives be provided – would we model these internally based on a gas/ASHP alternative heating system for a single property of similar size, or would costs / modelling be provided? How far back historically would prices need to go, and how would inflation etc. be factored in and communicated? Would these comparisons need to be provided to residents (aware that is more of a question for the future 'billing and transparency' consultation)?

4. Does the revised authorisation condition, 'fair pricing', reflect the policy intent?

Yes.

Market segmentation

5. In relation to market segmentation (please note that we are asking in relation to the considerations discussed in paragraphs 2.58-2.61, segmentation considerations in relation to price benchmarking are considered under Chapter 4: Price comparison and benchmarking methods):

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

In section 2.60, consideration of small network size should also consider the data privacy of customers; on small networks, customers may be identifiable as individuals from certain data on vulnerabilities.

Otherwise, yes.

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

Yes.

Data requirements

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

Charges:

- standing charges for heat (not separated out, but could be collected)
- unit rates for heat
- connection charges (not separated out, but could be collected)
- any other charges, for example one-off charges (not separated out, but could be collected. Note that large capital or maintenance bills may be smoothed out on customer bills over time, or may be taken on board by a social housing association and not passed on to customers, so as to be akin to the costs of replacing an individual property boiler not being directly charged to the resident.)

Prices:

- total annual charges across all consumers
- number of customers (to calculate mean annual customer bill)
- annual network demand (to calculate mean price per unit of heat delivered)
- reference prices: prices for consumers at reference usage levels (not currently collected, but could be done relatively easily if guidance on what suitable comparisons are and how comparisons should be made)

Cost Allocation:

- overview of costs recovered through standing charges (not separated out, but could be collected)
- overview of costs recovered through unit charges (not separated out, but could be collected)
- connection charging methodology (not currently collected, but could be done relatively easily)

Cost drivers:

- network supply heat price
- annual network demand
- annual network generation
- other efficiency measures
- number of customers
- type of network
- function
- profit or non-profit
- technology type
- ownership or commercial arrangements
- network built pre-regulation versus post-regulation
- zoning location
- metered versus non-metered

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

Cost Drivers:

- Operating temperature
- network length

Financial data:

- Data for collecting EBIT margins:
 - revenue
 - operating costs (expenses directly associated with running the heat network) including but not limited to fuel costs, operations and maintenance, administrative expenses, and depreciation

8. Of the cost drivers listed in Table 7 (in Appendix 3), which items would be more challenging for heat networks to report?

Network Demand (for unmetered properties)

Network length

Network generation (if not already known, would require a consultant to advise)

How will operating temperature be determined (within the boiler/plant room, at furthest point of network etc.)?

- 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?**

Non-metered networks will find network demand hard to provide.

Small networks (with limited number of customers) not to provide level of vulnerability, for risk of identifying individuals.

Cost Allocation

- 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?**

Yes.

- 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?**

Yes. Nothing else to add, or to strengthen to a prescriptive rule.

- 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?**

Un-metered and metered split seemed sensible in terms of the best practice approach.

- 13. Does the authorisation condition, 'cost allocation', reflect the policy intent?**

Yes.

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

N/A

Price comparison and benchmarking methods

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?

yes, though the issues in 4.14 and 4.15 could be resolved by providing an “average amount paid per consumer per year”, as well as providing the 20th and 80th (or equivalent) percentile.

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

Yes, but will this be a comparison as if the property were to be heated with an individual gas boiler or heat pump (i.e. one per housing unit, as if it were no longer on a heat network), or as if the heat network were to be powered with these as alternative technologies in the plant room?

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?

Yes. A model template could be provided, where the different factors are pre-populated, but can be altered to give more specific info on electricity prices, SCOP etc..

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?

Comparing within archetype groups could mean archetype groups where networks are all excessively priced go un-noticed. No additional drivers can be thought of.

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?

Network pipe length would be hard to measure for existing networks if not already known. Annual network demand will be hard to know for unmetered networks.

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?

Network generation will need an external consultant to advise on if not already known.

- 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?**

Agree with this approach.

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

In 4.51 and 4.52, for the “own past price benchmarking”, both an industry-led expected price increase and an organisational “expected price increase” should be provided in the comparison. If a heat network is locked into a procurement contract for a set period, during which time the market is volatile and increasing/decreasing, then benchmarking to industry-expected gas price changes may not be appropriate to reflect the benchmark.

Would the first submission of data require several years’ worth of costs/prices, to allow for the “own past price benchmarking”?

Profitability Analysis

- 23. Do you agree with the proposal for ongoing monitoring of profitability through data collection on EBIT margins for all heat networks?**

Yes, given the exception in 5.14 for heat networks that have declared as no-profit operators.

- 24. How challenging would it be for heat network operators and suppliers to provide the data outlined for calculating EBIT margins? What barriers, if any, might affect the accuracy and completeness of the data?**

N/A – our heat networks would be operating as non-profit due to serving social housing residents

- 25. As data collection improves, do you agree that more in-depth profitability assessments, for example using Return on Capital Employed (ROCE), should be conducted for networks identified as outliers through benchmarking?**

N/A – our heat networks would be operating as non-profit due to serving social housing residents

26. Do you have any other feedback on the proposed approach to profitability assessment?

N/A – our heat networks would be operating as non-profit due to serving social housing residents

Central Price Transparency

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.

Heat network end customers would need to be provided with all the details of the categories of their heat network on their bill, so that they can choose the correct grouping in option 1; they may not even be aware if it is gas powered or metered etc..

Option 1 is preferred, though could (as noted in the consultation) be combined with a RAG rating within the grouped comparisons, and/or the counterfactual of an individual gas boiler / heat pump (both for that specific heat network, and for the others within the grouping). Comparing the counterfactuals, as well as the heat network prices, may make it more obvious to customers/end users that the difference is due to the structure of their property, the set up of the heat network, or profiteering.

Until this is able to be set up, option 2 is preferred. Simply relying on RAG ratings as per Option 3 is fraught with risks of interpretation.

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?

Despite being how averages work, anything shown as “above average” will likely be interpreted as a disproportionately expensive bill, and so anything showing this will need clear wording around it.

Consumers should be presented with the information they need to be able to complete appropriate comparisons on every bill, and offline alternatives should be available too (e.g. showing a graph of suitable comparisons with an explanation on their annual bill).

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

I think a RAG rating within option 1 is the best approach, rather than viewing options in isolation.

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

Yes, Option 2, followed by Option 1 when data allow (with both utilising a RAG rating within them), would be a good approach.

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

Agree with this, but explanations for customers will need to be matched to make up for the simplified (and potentially misinterpreted) data representation.

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?

Agree, as most of this is covered in reporting requirements elsewhere in the consultation.

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

Yes, and think there is a space for using the counterfactual comparison with individual gas boilers / heat pumps as part of the transparency, to show if the price differences are due to the property type, the heat network, or profiteering.

Price Investigations

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

Yes. There is adequate time before it comes into force, and each case is assessed on its facts.