

Heat Networks Regulation Working Group

Interim Recommendations Report

December 2019

CONTEXT

1. On 22 November 2018, the Minister for Energy, Connectivity and the Islands announced that the Scottish Government would begin preparing legislation to introduce regulation to the heat network sector in Scotland¹, following two earlier consultations^{2 3}.
2. On 14 May 2019, the Minister invited stakeholders to form the Heat Networks Regulation Working Group to support the preparation of legislation, by using its expertise and experience to advise on a regulatory framework which the Scottish Government had developed.
3. During the course of the Working Group, the Scottish Government's Programme for Government confirmed that a Heat Networks Bill would be introduced to the Scottish Parliament (subject to the way in which the UK leaves the European Union).
4. The Working Group was also invited to make recommendations regarding other Scottish Government policy that it sees is key to supporting the regulatory framework, or which may otherwise support the deployment of heat networks in Scotland.
5. The Working Group was asked to consider the legislative competence of the Scottish Parliament. In summary, the following levers are devolved to Scotland:
 - **Building Standards:** we can set emission standards for heating systems and standards for overall energy use and environmental impact of buildings (new build and existing);
 - **Regulation of Heat (including Heat Networks):** technical standards, consenting, etc. (but not consumer protection);
 - **Grants, Loans and Advice Support Schemes:** for example, Energy Efficient Scotland, District Heating Loan Fund (DHLEF), Home Renewables Loans, etc. Home Energy Scotland & Resource Efficient Scotland advice services; and
 - **Innovation & Commercialisation Support:** such as the Low Carbon Infrastructure Transition Programme (LCITP).
6. Meanwhile, the following levers remain reserved to the UK Parliament:
 - **Gas Network:** standards and quality i.e. what goes through the pipes;
 - **Consumer Protection;**
 - **Price signals:** e.g. tax, levies and charges in relation to gas.

¹ **Official Report**, the Scottish Parliament, 22 November 2018:

<http://www.parliament.scot/parliamentarybusiness/report.aspx?r=11795>.

² **Consultation on Heat & Energy Efficiency Strategies, and Regulation of District Heating**, the Scottish Government, 24 January 2017:

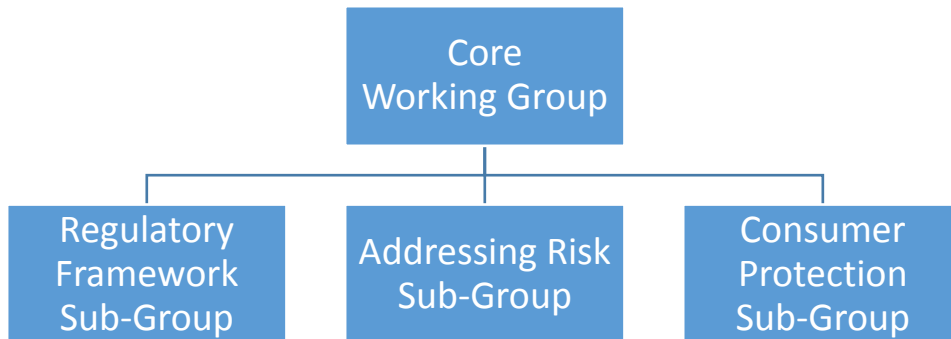
<https://www.gov.scot/binaries/content/documents/govscot/publications/consultation-paper/2017/01/consultation-heat-energy-efficiency-strategies-regulation-district-heating/documents/00513244-pdf/00513244-pdf/govscot%3Adocument/00513244.pdf>.

³ **Scotland's Energy Efficiency Programme: Second Consultation on Local Heat and Energy Efficiency Strategies, and Regulation of District and Communal Heating**, the Scottish Government, 14 November 2017: <https://www2.gov.scot/Resource/0052/00527606.pdf>.

APPROACH OF THE WORKING GROUP

7. Working Group members comprised stakeholders drawn mainly from the industry, consumer groups, local government and supply chain. Since the focus of the prospective legislation is to support the deployment of heat networks in Scotland, wider industry stakeholders were invited to one of the meetings. A full list of all contributors is at **Annex A**.

8. Members of the Working Group worked in three thematic subgroups, focusing on the regulatory framework; addressing demand risk and consumer protection. This was to enable Group Members' involvement to be focussed on those areas which were of most interest to them, or to which their expertise and experience were most relevant.



9. Each of the topics had a dedicated paper that was discussed by the stakeholders during sub-group meetings and at the Working Group plenary meetings. Comments made during the workshops, along with written comments from the Working Group members, were used to draft this Report. The Working Group's Key Findings are below, while further discussion of the three issues have been provided to the Scottish Government to support a draft Bill.

10. The Regulatory Framework Sub-Group considered:

- the creation of a sector regulator;
- the introduction of a licensing system;
- the introduction of a consenting system;
- conferring statutory undertaker rights; and
- the creation of a facilitation process to encourage heat network connections and/or the use of waste/residual heat.

11. The **Addressing Risk Sub-Group** considered whether further measures, both within and outwith the scope of primary legislation, could support the regulatory framework, above.

12. The **Consumer Protection Sub-Group** considered what safeguards are needed for heat network customers and whether any special considerations applied in Scotland.

KEY FINDINGS

Regulatory Framework

13. The Group agreed that the heat networks market would benefit from the introduction of a Regulator.

14. It was neutral on which body would be best suited for this role, but could see sense in a Scottish Regulator given that a counterpart in the wider UK has not been confirmed, the accelerated legislative timelines in Scotland and the additional functions likely to feature in the Scottish Regulatory framework.

15. However, the Group also agreed that should there be a Scottish Regulator, there should be alignment with any counterpart in the rest of the UK, as far as possible.

16. The Group supported the principle of introducing licensing to the sector, provided that this was balanced by sufficient measures to support developers and that licenses did not unduly burden smaller operators. Some Group members also advocated for a project-specific license to tailor standards and fees.

17. The Group briefly discussed Local Heat and Energy Efficiency Strategies (LHEES) and there was consensus that the requirement to produce Strategies should be made a statutory duty, subject to appropriate support for Local Authorities being put in place at a national level. It was also noted that, amongst others, heat network developers should be involved in the development of LHEES methodology to ensure that opportunities were fully identified and deliverable.

18. The Group felt that the consenting proposal should be reconsidered in order to reduce burden on both local authorities and network developers, and to reduce the risk of Local Authorities effectively self-regulating.

Addressing Risk

19. The Group welcomed the proposed introduction of LHEES and supported them being made a statutory duty. There was recognition that the creation of Heat Network Zones through LHEES would be a positive step for the market.

20. The Group also requested greater clarity over how heat network project identification and appraisal will be carried out as part of LHEES.

21. Despite the introduction of LHEES being welcomed (and despite heat network developers not being adverse to owning a degree of risk), they would not alone significantly change the risk profile for investors. More is needed within the framework of government support and legislation to support the growth of load which the market currently perceives to be uncertain and risky.

22. There were a number of suggestions on how to de-risk investment, and the Group felt that a combination of proposals and policies would be required to sufficiently de-risk demand. Such as:

- For heat network developers and other organisations to be able to compete to be awarded exclusivity within identified heat network zones;

- An obligation to connect to a heat network being placed on large anchor load non-domestic buildings within identified heat network zones to address decarbonisation of existing buildings as well as new build;
- That Scottish Planning Policy more strongly encourage connection to heat networks, both in new and existing buildings. The Scottish Government was asked to consider the 'London Hierarchy' model;
- Guarantees such as the 'demand assurance' model;
- Subsidy (to help compete against gas heating) for low-carbon inputs and some strategic infrastructure (e.g. joining of different schemes); and
- Using public procurement, taking account of total lifecycle costs, to ensure connections to heat networks.

23. It was agreed that statutory undertaker rights should be conferred on heat network developers and that this would be a beneficial change. However, it was noted that this, on its own, would not sufficiently de-risk investment in heat networks.

Consumer Protection

24. The Group had limited time to discuss in detail the specific consumer standards that should be introduced on a statutory basis. The Group was also challenged as it did not yet have clarity over who would be delivering any consumer standards in Scotland in future.

25. The Scottish Government assured that it recognised the extensive work done by Citizens Advice Scotland (CAS) and the Heat Trust in this area, as well as accepting the recommendations of the Competition and Markets Authority (CMA).

26. Key recommendations were as follows:

- The Group wants consistency of service standards across the UK, particularly if there will be separate regulators in Scotland and the rest of UK, in which case the Working Group recommended they are broadly in alignment.
- Pricing was identified as a one of the key issues, but the Working Group did not reach a conclusion on whether and how this should be regulated. However, publication of tariffs (including standing charges) and benchmarking were generally seen as being beneficial, while not-for-profit schemes were felt by some to likely hinder private sector investment.
- The Group felt that clearer communication from the Governments on the benefits of heat networks is essential to support uptake – particularly in light of the changes which will need to occur in response to the global climate emergency.

NEXT STEPS

27. The Group has carried out its initial remit in very short timescales, in light of the possibility of legislation coming forward in this area.

28. Now that a Bill has been confirmed in the coming year, the Working Group is at this stage providing an Interim Report to provide evidence and advice to the Scottish Government to inform its legislation.

29. However, there are several further areas in which the Group believes the Scottish Government could help to create a supportive environment for the sector to grow.

30. In addition to the key findings above, the Working Group recommends that a refreshed Group should to meet discuss wider policy. The Group noted that a refreshed remit could not be fully confirmed before further detail on the content of the Bill was provided. However, it was initially felt that issues to be discussed could include:

- Public funding for strategic network infrastructure and low-carbon heat generation;
- Non-domestic Rates;
- Planning policy;
- Building Standards/regulations;
- Procurement;
- Community engagement / ownership;
- Demand risk;
- Consumer protection; and
- LHEES.

31. It was also felt that the Group could provide a forum for: providing updates during the passage of the Bill; shaping subsequent regulations following the passage of the Bill; considering how to support smaller, existing networks with the impacts of regulation being introduced; and engagement between government and those working in the sector commercially to understand how policies work in practice in the development of heat networks.

ANNEX A: WORKING GROUP MEMBERSHIP

Aberdeen Heat & Power
Angus Biofuels
Citizens Advice Scotland (CAS)
City of Edinburgh Council
Energy Saving Trust (EST)
Engie
Heat Trust
Highland Bioheat
Historic Environment Scotland
Scottish Futures Trust (SFT)
Scottish Renewables
SSE
Stirling Council
The Association for Decentralised Energy (the ADE)
The Chartered Institute of Building Services Engineers (CIBSE)
The Competition and Markets Authority (the CMA)
The Danish Energy Agency (the DEA)
The Scottish Environmental Protection Agency (SEPA)
The Scottish Federation of Housing Associations (SFHA)
Vattenfall

Ofgem (Observer)
The Convention of Scottish Local Authorities (COSLA) (Observer)
The Department for Business, Energy and Industrial Strategy (BEIS) (Observer)



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