

Heat Act 2: key points for investors

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Introduction

The draft Heat Act 2 was open for consultation until 3 August 2020. This draft bill – which will fundamentally change the regulatory framework for district heating compared with the current Heat Act – aims to advance the energy transition from gas to heat and thus help to fulfil the Dutch Climate Agreement's aims of a 49% reduction in greenhouse gas emissions by 2030 (with 1990 as the benchmark year). Further, the draft bill aims to:

- stimulate the scale-up of collective heat systems;
- provide a more transparent tariff scheme; and
- refine various conditions to safeguard security of supply.

The draft bill regulates, among other things:

- the roll-out of collective heat systems;
- the designation and obligations of heat companies and heat transport operators;
- tariff regulation;
- CO₂ reduction standards; and
- the key role of municipalities.

Heat plots and monopoly of heat transport and supply

Under the draft bill (and the Dutch Climate Agreement), the country's municipalities must take the lead in making district-oriented plans regarding the establishment of collective heat systems. These plans are set out in policy documents such as the heat transition outlook, which is a product of a participatory process of different stakeholders (ie, citizens, local governments and utilities). The heat transition outlook (which is not governed by the draft bill) determines, among other things, how many houses and other buildings within the municipality will be insulated or disconnected from natural gas by 2030.

Based on its heat transition outlook, the municipal executive will specify heat plots which can be situated in one or more municipalities and within which houses and other buildings will be connected to a collective heat system. In specifying a heat plot, the municipality will consider the principles of efficiency and supply security.

Heat company

After a heat plot is mapped out, the municipal executive (after a pre-assessment by the Netherlands Authority for Consumers and Markets (ACM)) will designate a heat company that will bear an integral responsibility for the construction, management and maintenance of the collective heat system and the efficient transport and supply of heat within the heat plot (for a minimum of 20 years and a maximum of 30 years). The heat company must develop a plot plan which outlines:

- the design of the collective heat system;
- the planning;
- the manner of participation; and
- the costs and tariffs.

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Further, the plot plan must pay attention to sustainability and supply security. The heat company must also develop an investment plan which will require the ACM's approval.

The monopoly of heat transport and supply within a heat plot has been heavily criticised and deviates from the strict separation of transport and supply prescribed for the gas and electricity markets. The government is of the view that the chances for a competitive market for local heat sources are slim and that it is therefore more important that heat be provided by specialised integrated entities which are governed by sector-specific regulations that guarantee the reliability, affordability and sustainability of heat.

A heat company may transfer the designation decision after the prior approval of the municipal executive.

Heat transport operators

The Minister of Economic Affairs and Climate Policy may, upon application, designate (for a minimum of 20 years and a maximum of 30 years) a heat transport operator for an existing or future regional heat transport network. A separate heat transport operator is the exception to the rule of integrated heat companies. The designation of a heat transport operator is envisaged where the amount of regional heat sources exceeds the local demand for heat. In that situation, a heat transport operator can make these heat sources available for multiple collective heat systems and large consumers (eg, the horticulture sector).

Transitional law

The area where a collective heat system is located on the basis of a decision or an agreement (eg, a concession) will qualify as a heat plot. Further, a heat company that has obtained the right to transport and supply heat on the basis of a decision or an agreement will be considered the designated heat company. If the heat company obtained the right to transport or supply heat for more than 30 years (or even an indefinite period), this period will be limited to 30 years. Conditions attached to the decision or agreement will be incorporated in the designation decision unless they are in breach of the Heat Act 2.

Small collective heat systems

The draft bill includes a ban on transporting and supplying heat by any party other than the designated heat company for a specific heat plot. There are several exemptions to this ban.

No heat company need be assigned for:

- very small collective heat systems that transport and supply heat to a maximum of 10 small consumers collectively; or
- small collective heat systems that transport and supply heat to a maximum of 10 natural persons or legal entities which each have an individual connection of a maximum of 100kW and which jointly purchase heat from their lessor, homeowners association or comparable entity.

Further, the municipal executive may grant an exemption from the obligation to be designated as the heat company (for a minimum of 20 years and a maximum of 30 years) for a small collective heat system (maximum of 500 consumers).

Sustainability

Under the draft bill, for every collective heat system, heat companies must comply with a minimum performance standard for CO₂ reductions. Every year, a minimal reduction will be set with the aim that all heat will be CO₂ free by 2050.

Structural non-compliance with the CO₂ reduction standard can have major repercussions. If the standard has not been met five years from the initial non-compliance, the ACM will notify the municipal executive, which will be obliged to revoke the designation decision.

New tariff scheme

Under the current Heat Act, the ACM sets maximum tariffs which are tied to the price of natural gas. The so-called 'no more than otherwise' (ie, no more expensive than natural gas) principle, which has a strong focus on consumer protection, is considered obsolete because it does not reflect the actual costs of heat companies, meaning that such companies' returns tend to be low. Consequently, the current tariff scheme negatively affects the scale-up of collective heat systems and, as such, the energy transition.

The draft bill abandons the no more than otherwise principle and switches to cost-based tariffs. The future tariff scheme focuses on allowing heat companies a reasonable maximum return and provides for efficiency incentives by benchmarking. In order to prevent tariff shocks, the transition to the new tariff scheme will be gradual.

A new element of the tariff scheme is that the supply of heat to large consumers will also be regulated to some extent. A heat company may set its own cost-based tariffs for large consumers, which must be checked by a certified public accountant.⁽¹⁾ The tariffs must be transparent, non-discriminatory and based on a reasonable return. The ACM will oversee this. In any event, the large consumer need not pay more than the maximum tariff on the basis of which it decided not to opt out during the first five years.⁽²⁾

Additional requirements for heat supply agreements

The draft bill includes additional requirements for heat supply agreements, such as:

- a description of the goods and services and the agreed quality standards (ie, the minimum and maximum temperature of the heat, the kind of heat and the tariffs and conditions);
- a description of the refund scheme if the quality standards are not met;
- the requirements of the indoor installation;
- the insulation value and characteristics of the ventilation system in order to be able to heat the accommodation to a minimum interior temperature of 20 degrees Celsius; and
- information pertaining to the possibility to submit a dispute to an independent arbitration committee.

If the heat company wishes to change its tariffs, it must inform its consumers in a timely and sufficient manner. However, it need not notify each consumer personally. The draft bill also stipulates that the heat company must provide its consumers with a specified invoice at least once a year. The invoice must contain information about the amount of consumed heat and the different cost items and indicate where the consumer can direct any questions and complaints about the invoice.⁽³⁾

Heat production

Obligation to provide heat company with residual heat

On request, a producer of residual heat must make the residual heat available to the heat company free of charge. The heat company must make this possible and will pay only the costs of:

- altering the installations;
- constructing pipes, installations or tools; and
- maintaining the supply security of residual heat.

Disputes pertaining to costs can be submitted to the ACM.

Change of control

A producer of (residual) heat which provides heat to a heat company must notify the minister beforehand of a 'change of control' (within the meaning of Section 26 of the Competition Act) pertaining to an installation with a capacity of more than 20MW.

Comment

During consultation, the draft bill received 101 responses. From these responses, it follows that many companies and interest groups are critical about the far-reaching market regulation, and some deem elements of the envisaged system (eg, the monopolistic position of the heat company and the heat transport operator) too rigid. It remains to be seen whether the responses and ongoing lobbying will lead to any significant changes. The Heat Act 2 is expected to enter into force on 1 January 2022, but this may prove ambitious in view of the criticism that the draft bill has received and the 2021 elections. Investors should closely monitor the legislative developments in the coming months.

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Endnotes

(1) The same system applies to small collective heat systems.

(2) Large consumers (with a connection of more than 100kW) must state that they do not want to be connected to the collective heat system (ie, opt out) prior to the amendment of the future environmental plan on the basis of the future Environmental Planning Bill, which is expected to enter into force by 1 January 2022.

(3) Implementation of EU Directive 2012/27/EU of 25 October 2012.