

# Heat networks regulation: fair pricing protections

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## About Energy UK

Energy UK is the trade association for the energy industry, representing companies investing billions of pounds to secure our country's current and future energy needs. From growing start-ups to major electricity generators, grid and infrastructure developers and energy suppliers, our members are driving change across power, heat, transport and flexibility. We provide a collective voice for the sector working with governments, regulators, charities and other organisations to provide crucial insight that shapes policy, offers solutions and promotes best practice.

## Executive Summary

The implementation of consumer protections, including pricing regulation, in the heat networks sector is essential to tackling consumer detriment. When it comes to pricing, [research by Citizens Advice](#) has found that unfair billing practices, and large bill increases are affecting some heat network households. Pricing practices and customer service need to improve dramatically in the sector to enhance the reputation of heat networks and provide investor confidence that enables the sector to grow at pace in the years ahead.

Energy UK supports the continued development of iterative and outcomes-based regulations, based on principles and supported by guidance. Outcomes-based regulations allow differentiation in the provision of services that creates benefits for all customers, as services can be tailored to best meet their needs.

Across the board, it is important that regulation is developed and introduced in response to evidenced consumer detriment. However, there is a lack of reliable quantitative data about current practices in the sector, as demonstrated by the consultation's citation of the [Competition and Market Authority's \(CMA\) 2018 market study](#), which did not find evidence of systemic high prices in the sector, and the reference to inputs into Ofgem providing only anecdotal evidence to the contrary.

Energy UK is concerned that more information is needed before the framework is further refined so that it works for both the existing sector and new, modern, city-scale networks. Some elements of the proposed regulations in this consultation are at risk of being overly complex and restrictive without there being the data available to evidence consumer detriment, and therefore demonstrate how the regulations would generate consumer benefit.

Ofgem and industry have a shared responsibility to co-design a consumer protections framework that minimises avoidable regulatory burden, as this reduces the associated resource requirements on both the regulator and business community, and ultimately reduces systems costs paid for by consumers.

The additional detail on the 'Fair pricing framework' provided in this consultation is welcome. It is also positive that several points made in [Energy UK's response to the January 2025 Department for Energy Security and Net Zero \(DESNZ\) and Ofgem](#) consultation on implementing consumer protections have been taken forward, for example market segmentation depending on the type of network, and ensuring that both domestic and non-domestic customers can benefit from the regulations. In this response, Energy UK called for a long-term view of fair pricing, and more detail on how this could be implemented is included in this response.

It is important to note that the implementation of these regulations from January 2027 is fast approaching. This leaves a shrinking window of time for Ofgem to reflect on the feedback provided, and engage where appropriate in further consultation with industry and consumer representatives. Energy UK is particularly concerned about this, as there are numerous proposals within the consultation that it believes need to be revisited, for example the approach to price comparison and benchmarking methods, and central price transparency. More detail is provided in the responses below.

For the regulation to be effective, the consumer protections framework needs to be considered in the context of future trajectories of heat decarbonisation and electrification. In practice, this means that the development of regulation must be underpinned by progress on the rebalancing of policy costs for non-domestic electricity customers, as the current arrangements mean that households supplied by new, low-carbon heat networks may face higher bills than their counterparts on gas. While progress on rebalancing in the Industrial Strategy was positive for certain sectors, [Energy UK has put forward proposals](#) for rebalancing to cut costs for Great British business energy customers across the board by up to 15%.

Another opportunity to adopt an effective approach within the regulations is to focus the price comparison methodologies on the relevant counter-factual, based on equivalent carbon emissions. Low-carbon heat network prices should be compared with other low-carbon heating technologies, while traditional gas Combined Heat and Power (CHP) systems should be compared with other gas customers.

Finally, the pricing framework should be developed in the context of wider heat network regulatory development, including heat network zoning and the heat networks technical assurance scheme (HNTAS).

Energy UK believes a single body, Ofgem, should have oversight of pricing. DESNZ recently consulted on proposals for windfall profit-sharing within zones and under current proposals the Zoning Coordinator will have responsibility for monitoring and enforcing pricing conditions at a local level. This proposal risks duplicating pricing

policy and regulation across multiple organisations, which could create confusion for industry and consumers.

Ofgem's proposals for the fair pricing framework appear to require heat networks to demonstrate cost efficiencies through technical improvements. However, these requirements should already be addressed under HNTAS, which will provide a mandatory and comprehensive framework for technical standards across all heat networks, and which will be overseen by Ofgem. Therefore the proposals in this consultation should be considered in the context of wide heat networks regulatory development.

Significant work has been undertaken by both DESNZ and Ofgem to develop the policy proposals this far, and Energy UK supports and welcomes these efforts, however it feels that further work is needed on the design of the Fair Pricing Framework so that it supports investment while protecting consumers. Energy UK and its members are ready to work with Ofgem to help adapt these proposals.

## Consultation response

### Fair pricing framework

**Q1. 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.**

Energy UK supports the objective, principles and outcomes and supports the definitions.

**Q2. 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.**

Energy UK supports the identified areas to be included in the fair pricing principles implementation guidance.

**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.**

Cost reflective pricing – there will be a range of approaches including district heating schemes supplying to buildings, and secondary heat networks. The guidance should be high level to reflect the broad range of ways that heat networks structure their pricing. One example is that a heat network may set its prices on a portfolio basis. In this case, the tariff structure is not solely linked to an individual heat network's underlying cost base. It is not clear how this pricing structure will be assessed under the Fair Pricing Principle.

Energy UK recognises that there is an important balance in socialising the fixed costs of heat networks on a portfolio basis, and charging consumers based on usage profiles. As more data is collected on pricing practices, the guidance can be iterated to potentially provide more prescriptive guidance on 'cost reflective pricing' to market segments where consumer detriment is found.

Procurement good practice – this guidance would benefit from a market segmentation approach. Heat networks run by building owners on a not-for-profit basis will be operating differently to district heating schemes. For district heating schemes, the guidance should be high level as approaches to procurement are commercially sensitive and variable based on business strategy.

Guaranteed Standards of Performance (GSOPs) - support these payments as restricted cost passthrough at this stage in the iterative regulation process.

Fair and reasonable returns – greater clarity on what constitutes an 'unusually high' return would be beneficial, as this will help improve confidence for consumers and investors.

The reference to external shocks is welcome, and the challenges suppliers will face in managing short-term affordability issues, as they experienced during the recent gas price crisis.

### **Q3. 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.

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

Energy UK supports the approach by Ofgem to implement the fairness test in terms of objectivity and adopting a case-by-case approach.

### **Q4. Does the revised authorisation condition, 'fair pricing', reflect the policy intent?**

Energy UK supports this wording.

**Q5. 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?**

Energy UK does not support pre-legislation networks having a longer transition period on data reporting requirements, as this will create data and regulatory asymmetry.

Customers of shared ground loops (SGLs) will have electricity meters, rather than heat meters, however they will pay network charges. The fair pricing framework should be proportional to this arrangement.

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

Overall, segmentation is helpful as it recognises the large range of variables within the heat networks sector. However, it is only needed where a specific protection is not relevant to a given network.

Zoning location - there is insufficient detail shared on how heat network zoning may impact on Ofgem's implementation of the fair pricing framework. Energy UK is clear that there should be a single regulatory approach to pricing, and that this should sit with Ofgem. This would provide a more consistent regulatory environment, which will help attract investment into the sector. Consumers will benefit from fair and proportionate prices through the Ofgem regulations.

**Q6. Of the information listed in Table 3 below, what do heat networks already regularly collect and can be easily reported?**

Energy UK members will respond individually to this question.

**Q7. Of the information listed in Table 3 below, which items would be more challenging for heat networks to report?**

Energy UK members will respond individually to this question.

**Q8. Of the cost drivers listed in Table 7 (in Appendix 3), which items would be more challenging for heat networks to report?**

Energy UK members will respond individually to this question.

**Q9. 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?**

Ofgem and industry have a shared responsibility to co-design a consumer protections framework that minimises avoidable regulatory burden, as this reduces

the associated resource requirements on both the regulator and business community, and ultimately reduces costs to consumers.

Data provision is one area in which Ofgem could look to streamline the requirements on business, balanced against the need to monitor consumer experience and business practices. For example, many of the data points listed in the consultation are unlikely to change as frequently as they are being requested. The number of customers, annual network demand, and connection charges will not often change on a quarterly basis.

### **Cost allocation**

**Q10. 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?**

Agree.

**Q11. 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?**

Overall, Energy UK supports the draft best practice guidance and disagrees that it should be strengthened to prescriptive rules. However, this may need to be iterated for some market segments if evidence of consumer detriment is found once the regulations are in place.

While prices should be cost reflective, there should also be incentives for heat networks to drive efficiencies. Avoiding prescriptive rules enables innovation in tariff design. For example, a heat network may develop a tariff structure that incentivises energy efficiency.

**Q12. 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?**

Energy UK supports avoiding a one-size fits all approach as this would not suit the diversity of different business models in the sector. The guidance should be positioned as a best practice resource, rather than creating de-facto prescriptive regulation.

**Q13. Does the authorisation condition, 'cost allocation', reflect the policy intent?**

Yes.

**Q14. What other feedback do you have on the proposed approach to cost allocation?**

The consultation notes concerns that early users of a heat network may be exposed to higher costs as they pay a disproportionate share of upfront capital costs.

To help address this, the Government could look at developing a price support mechanism for early users of new, low-carbon heat networks. This could be a ringfenced support mechanism that provides funding to help bridge the gap between costs and returns as demand assurance is built. This could be in place until non-domestic rebalancing has been implemented, and clean heat is the cheapest form of heat. Alternatively, once a critical mass of customers connects, then this mechanism can be withdrawn as the network costs and capital cost recovery will be shared by a greater number of consumers, including large non-domestic customers.

### **Price comparison and benchmarking methods**

#### **Q15. 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?**

The price should be defined as the total effective price that the customer pays per year, with some nuance based on usage or defined alongside an indication of average consumption across the network.

It is important that the Government presses ahead with the unbundling of heat and rent or service charges, as consumers risk falling through the gaps in consumer protections while this practice continues. DESNZ should work with MHCLG to expedite this process.

#### **Q16. Do you agree with our proposal to use gas boilers and heat pumps as external reference benchmarks?**

Agree.

The low-carbon counter-factual is the most relevant counter-factual for newly developed low-carbon heat networks. Gas is the most relevant counter-factual for traditional gas-fired Combined Heat and Power (CHP) units. Ultimately, when assessing and determining fair pricing, the regulator should use the most appropriate counter-factual for a network in terms of carbon emission levels.

It should also be noted that some heat networks provide cooling, and consideration is needed for how this will be treated within the benchmarking.

The consultation notes that a gas benchmark will become less relevant as wider heating decarbonisation takes effect. The regulations should be suitably flexible to adapt the counter-factual as the clean heat transition progresses, and in response to further policy development, such as the rebalancing of policy costs on energy bills.

It may be beneficial to explore electric panel heaters and electric storage heaters as a counter-factual, as these are referenced [in the recent Boiler Upgrade Scheme expansion consultation](#) for space-constrained properties, and where heat networks present a viable and efficient low-carbon alternative, as well as air-to-air heat pumps and heat batteries which represent further low-carbon counter-factual options.

**Q17. 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?**

It may be worth adding air-to-air source heat pumps, as changes to the Boiler Upgrade Scheme may lead to an increase in these installations in space constrained properties, so they therefore are a relevant counterfactual for heat networks.

**Q18. 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?**

In Energy UK's submission to the DESNZ review of Ofgem, it called for Ofgem to protect current and future consumers through a forward-looking approach. Overall, the benchmarking approaches proposed in the consultation risk being excessively complicated and resource-intensive for Ofgem without any clear additional consumer benefit beyond that which is provided by counter-factual benchmarking.

Counter-factual benchmarking can show whether a price is disproportionate relative to the equivalent carbon emissions alternative. This comparison is more meaningful for a customer than the price that they are paying compared to other heat networks, which they cannot connect to, and the past prices charged by a heat network which will represent a different set of circumstances (e.g. perhaps a different form of generation or number of customers served by the network), and which again cannot be changed, without significant investment and over a long period of time.

Furthermore, comparisons between different networks ('grouped comparison') have limited value owing to variables such as geographic differences which affect how the pipes can be laid in the ground, or the variety of heat sources available. This all impacts the underlying costs. Price transparency should be presented in a clear and accessible way for customers without requiring detailed explanation of these nuances. This approach risks misrepresenting fair and justifiable prices.

Energy UK is calling for Ofgem to review the proposals for benchmarking. Ofgem should consider introducing a simpler approach whereby an appropriate threshold is set for each group of heat networks, depending on the equivalent carbon emissions counter-factual. Where prices are being charged by the heat network above this threshold, then Ofgem should undertake further investigation based on the other methodologies set out in this paper, such as the sharing of EBIT data on an individual network level, or collecting data on cost drivers of that network.

**Q19. 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?**

Energy UK members will respond individually to this question.



**Q20. 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?**

Energy UK members will respond individually to this question.

**Q21. 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.

**Q22. Do you have any other feedback on the proposed approach to price comparison and benchmarking?**

Streamlining the data requirements within the price comparison section of the regulation is a potential area in which Ofgem could minimise regulatory burden, without negatively affecting consumer outcomes.

Energy UK sets out an alternative approach to benchmarking in its response to question 18. If a heat network is not found to be charging disproportionate pricing relative to the appropriate counter-factual threshold, then there is limited consumer benefit to Ofgem collecting data on cost drivers for that particular network. The data should instead be collected from networks that are found to be charging disproportionate prices, so that Ofgem can start to build a picture of causes of unfair prices in the sector.

### **Profitability analysis**

**Q23. Do you agree with the proposal for ongoing monitoring of profitability through data collection on EBIT margins for all heat networks?**

Energy UK does not support this proposal. EBIT should be assessed on a portfolio basis, as this will enable businesses to balance costs and prices across the heat networks within their portfolio, as some heat networks socialise costs in this way.

EBIT also needs to be sensitive to different revenue models, for example which may involve lower revenues in the early years and higher revenues in the later years to recover initial shortfalls and deliver returns for capital investors. The customer may be paying the same price, but the network’s profitability could be different depending on the stage at which the revenue model is at.

EBIT data should be collected on an individual heat network basis only where Ofgem is required to conduct further investigation, after it has found evidence of disproportionate pricing through the benchmarking process, as described in Energy UK’s response to question 18.

This approach would be inconsistent with other regulated markets. The focus should be on efficiency, including technical and administrative efficiency.

**Q24. 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?**

Energy UK members will respond individually to this question.

**Q25. 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?**

Energy UK supports this approach for outliers.

**Q26. Do you have any other feedback on the proposed approach to profitability assessment?**

None.

### **Central price transparency**

**Q27. 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.**

Energy UK supports the objectives of central price transparency to provide confidence to heat network customers that they are being charged a fair and reasonable price for their heat. Transparency in this way should be designed to build consumer confidence in the sector, as this will enable it to grow in the years ahead.

Energy UK has concerns that Options 1 and 3 risk misrepresenting fair and justifiable prices.

Option 1, the 'grouped comparison', potentially lacks meaning for customers given the large number of variables and cost drivers that determine a price that a heat network sets. This could include geographic differences, access to different heat sources, and strategic decisions that heat network companies take about socialising prices. Furthermore, if high pricing is embedded within a particular group, then no pricing investigation would be taken forward.

Option 2, 'market average/comparison to counterfactual', is the most suitable approach to be taken forward. Counter-factual benchmarking can show whether a price is disproportionate relative to the equivalent carbon emissions alternative. This comparison is more meaningful for a customer than the price that they are paying compared to other heat networks, which are not comparable for the reasons of high variability, described above.

Option 3, 'RAG rating', risks oversimplifying highly complex pricing structures without appropriate nuance.

Irrespective of the final methodology taken forward, Ofgem should work closely with Citizens Advice and Consumer Scotland so that these consumer advocates can create guidance and support to help consumers interpret this data.

This information should also be provided in the broader context of the transformation that the sector is undergoing, and that regulation takes time to influence pricing practices and customer service. Broader context should also be supplied around the clean heat transition, and the economic and system values of new city-wide, low-carbon heat networks.

A consideration that is potentially missing from this part of the consultation, is what the customer can do if they feel that their prices are unfair. Ofgem should start from the point of what a good consumer outcome is for someone challenging their price and then design the central price transparency regulations from this starting point.

Energy UK has concerns that if a heat network customer challenges their price, the network owner has limited recourse to either explain or reduce the price. The network will not know the details of the comparator price and, therefore, will not be in a position to explain the different cost drivers. Investing in improving the efficiency of the network to reduce the price will take years to implement, and the cost of these improvements will be recouped on bills, unless Government grant funding is available.

Overall, some of these approaches risk causing unnecessary reputational damage to the industry and hindering investment at a time when the sector is primed to grow at pace. Heat networks are anticipated to meet 20% of space heating demand by 2050, and [industry has ambitions to invest £80 billion](#) in the process. The current proposals risk misrepresenting prices in the sector and leaving dissatisfied customers with unresolved complaints.

It may be beneficial for Ofgem to work with industry to develop high level guidance around a triage route for customers, to address their pricing concerns. The heat network would need to resolve these in the first instance, but with customers ultimately being referred to the Energy Ombudsman, depending on number, sizes and level of detriment.

**Q28. 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?**

Energy UK supports an appropriate iteration of Option 2.

There should be as little burden as possible on consumers to interpret the information, and Ofgem should work closely with Citizens Advice and Consumer Scotland so that these consumer advocates can create guidance and support to help consumers interpret this data.

**Q29. Do you support focusing on one option or a combination of options in paragraph 6.69?**

Energy UK believes that the Heat Cost Calculator would be the most straight forward option for consumers to understand. However, this should be based on Ofgem-commissioned consumer research to identify the most appropriate option depending on the feedback from consumers who will use this.

**Q30. Do you support the phasing in of the options described in paragraph 6.70?**

The decision to phase in should be informed by Ofgem-commissioned research into consumer preferences, and the decision made based on the outcomes of this research.

**Q31. Do you support the adoption of different options for different heat network groups described in paragraph 6.71?**

Adopting a diversity of different approaches to central price transparency risks adding further complexity from the perspective of the consumer.

**Q32. 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?**

Energy UK members will respond individually to this question.

**Q33. Do you think it is appropriate to link central price transparency with benchmarking?**

Yes.

Energy UK's view is that a benchmarking approach whereby the prices that heat networks are charging compared to the equivalent counter-factual on a carbon emissions basis would be appropriate to link to central price transparency.

In this scenario, a consumer on a low-carbon heat network would be able to compare their annual bills to that of a heat pump user, perhaps on a similar usage profile, and see if their prices were too high, or about right.

## **Price investigations**

**Q34. Do you agree with the approach to price investigations set out so far? Please provide reasons and views to support your response.**

Yes, Energy UK supports this approach.

It will be beneficial for Ofgem to conduct thorough internal checks as part of its price investigations given the level of complexity and granular data points being monitored under this framework.

