

## Decision

# Heat networks regulation: price protections draft guidance decision

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Publication date: 13 January 2026

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Team: Heat Networks

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Email: [heatnetworksregulation@ofgem.gov.uk](mailto:heatnetworksregulation@ofgem.gov.uk)

In the [Heat networks regulation: fair pricing protection guidance consultation](#) ('2025 fair pricing guidance consultation'), we consulted on draft fair pricing and cost allocation guidance.

The consultation built on our joint consultation with the Department for Energy Security and Net Zero (DESNZ) Heat networks regulation Implementing consumer protections consultation ('[2024 ICP Consultation](#)').

This document outlines our decisions on these proposals following consideration of the responses to our consultation.

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## Executive summary

The Energy Act 2023 named Ofgem as the regulator for heat networks in England, Scotland, and Wales (Great Britain). [Our Forward Work Plan](#) outlines the work we are doing in 2025 and 2026, including our ongoing preparations for our new regulatory responsibilities for heat networks and the commencement of the new regime in January 2026.

Ofgem is introducing heat network regulation for the first time, marking a key step towards a fair and transparent market. Our priority is to understand the sector and lay strong foundations for long-term standards.

We are taking a principles-based outcomes-focused approach that balances flexibility for operators with improvements for consumers. Our aim is proportionate pragmatic regulation that supports compliance and good practice without unnecessary burden.

As the market matures and evidence grows, we will refine and strengthen the framework. The goal is to deliver good outcomes for heat networks consumers – fair treatment, transparent information, reliable service and fair prices. The Authorisation Conditions underpinning this regime are designed to be proportionate, cost-effective and drive improvements in consumer outcomes while supporting investments.

This document provides a response to the feedback received as part of our Heat networks regulation: fair pricing protection guidance consultation ([“2025 fair pricing guidance consultation”](#)) and accompanies the publication of our final fair pricing and cost allocation guidance (see ‘2025 fair pricing guidance’ under related publication links).

We also outline within this document our decision to update the “affordability” principle and rename it “consumer impact” to better reflect its intended purpose and contents.

## Response Overview

In general, stakeholders were supportive of our approach to the fair pricing and cost allocation guidance, noting that a flexible approach is required given the level of maturity of the sector and the initial phase of the introduction of regulation. Several stakeholders also commented positively on the proportionate approach taken.

However, stakeholders requested further clarity on some of the definitions and further insight into practices that would be deemed acceptable or unacceptable under the framework and cost allocation. Respondents highlighted the need for further guidance, requesting the provision of practical examples and best practice documents to support their understanding of how to comply with the principles set out in the guidance. Some also sought more tailored guidance for specific segments of the market, such as not-for-profit and unmetered networks.

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In particular, the question of what constitutes fair and reasonable returns generated extensive feedback. Several stakeholders sought further clarity, while a few expressed strong reservations about our proposals. We support heat networks earning a fair return that reflects investment risk, performance, and their capital-intensive nature, while ensuring consumer protection. To better understand market dynamics, we will monitor profitability across the sector, recognising the limitations of this approach and that high profitability does not necessarily indicate disproportionate pricing. Efficiency improvements should deliver benefits for both consumers and businesses.

Respondents raised concerns regarding overlaps with the Heat Networks Technical Assurance Scheme (HNTAS) and interactions with the Landlord and Tenant Act 1985. We recognise the interaction with HNTAS and are continuing to collaborate with DESNZ on this. We acknowledge that the framework may need to consider existing housing legislation and this has been considered when drafting the guidance.

Heat network regulation has complex interactions with housing legislation across GB, and we are continuing to work with stakeholders to ensure we understand these and are aware of how any proposed reforms in housing could have impacts for heat network regulation. We have been working with industry and across government to understand the interaction with existing Landlord and Tenant Act. As part of the Heat networks regulation: implementing consumer protections Government response ('[2025 ICP government response](#)'), DESNZ set out that they are working with the Ministry for Housing, Community, and Local Government (MHCLG) , as well as the Welsh and Scottish Governments, closely to further explore options for unbundling heat charges from housing charges.

## Introduction

### Context

The [2018 CMA \(Competition and Markets Authority\) study](#) conducted into heat networks did not find evidence of systemic high prices across the market, compared to those paid by consumers on gas or electricity, nor did it identify at that time an urgent need for intervention to reduce prices. However, the CMA study did recognise there were some pockets of higher pricing and recommended that the sector be regulated, that the regulator should monitor prices to ensure they were not excessive and that the regulator should require that all heat networks comply with ‘principles-based’ rules or guidance on pricing. However, we recognise that there have been wholesale energy price rises since the CMA study was published which may have significantly impacted this market, and not all the findings from 2018 may still be valid today. We have also received more recent anecdotal evidence of high prices in the market.

The government expects the sector to grow rapidly in the coming decades, and we are committed to facilitating that growth, whilst ensuring good consumer outcomes and standards across the sector.

Our fair pricing policy, as outlined in previous consultations, seeks to achieve good consumer outcomes, such as reliable heat and good customer service, at a fair price, whilst balancing good industry outcomes, such as sector growth. We aim to achieve the consumer outcomes whilst also improving transparency and ensuring that consumers are protected from disproportionate pricing and monopoly power through an outcome-based approach. This approach also supports growth and investment in a nascent market by recognising variation across the sector and providing proportionate, largely non-prescriptive guidance.

Our primary focus is addressing pricing issues where these arise, whilst keeping any burdens on heat networks to a proportionate level. Our approach aims to balance consumer protection, through ensuring they are not subject to disproportionate pricing, with minimising regulatory burden on heat networks, such that the cost of compliance does not itself significantly increase customer bills.

In addition to protecting against instances of disproportionate pricing, our fair pricing guidance, along with our data reporting initiatives, will help us identify if there are systemic issues of disproportionate pricing in the market. This will also inform future policy development.

In August 2023, a joint consultation was conducted by Ofgem and DESNZ on Heat networks regulation – consumer protection to inform secondary legislation and Authorisation Conditions ([‘2023 consultation’](#)). An additional joint consultation, the [2024 ICP consultation](#), was launched building upon the 2023 consultation.

In these consultations and the subsequent government response, we outlined the policy proposals of the fair pricing framework.

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These proposals were developed further in two recent Ofgem consultations, the November 2024 Heat networks regulation: authorisation and regulatory oversight ([‘2024 ARO consultation’](#)), which sought views on definitions, registration processes, and data, and the [‘2025 fair pricing consultation’](#).

In September 2025 we published and consulted on our first draft guidance document, focusing on the topics of fair pricing and cost allocation, to seek specific feedback on our issued guidance from stakeholders.

## References to previous publications

This document makes references to the following previous consultations and government responses:

The ‘[2020 consultation](#)’ refers to the Heat networks: building a market framework consultation published in 2020, which informed the provision in the Energy Act 2023. The subsequent government response is referred to as the [‘2021 government response’](#).

The ‘[2023 consultation](#)’ refers to the Heat networks regulation: consumer protections consultation published in August 2023, which informed the Heat Networks Market Framework Regulations SI (2025 HNMFRGBR SI). The subsequent government response is referred to as the [‘2024 government response’](#).

The ‘[2024 ICP consultation](#)’ refers to the Heat networks regulation: implementing consumer protections consultation published in November 2024. The subsequent government response is referred to as the [‘2025 ICP government response’](#).

The ‘[2024 ARO consultation](#)’ refers to the Heat networks regulation: authorisation and regulatory oversight consultation published in November 2024. The subsequent decision document is referred to as the [‘2025 ARO decision’](#).

The ‘[2025 fair pricing consultation](#)’ refers to the Heat Networks regulation: fair pricing protections consultation published in April 2025. The subsequent response document is referred to as the [‘2025 fair pricing response’](#).

The ‘[2025 fair pricing draft guidance](#)’ refers to the Heat networks fair pricing and cost allocation draft guidance. The accompanying consultation that this document is responding to is referred to as the [‘2025 fair pricing guidance consultation’](#).

The final guidance that will be published alongside this response will be referenced as ‘2025 fair pricing guidance’.

## Our decision-making process

We received 38 responses to our consultation. We asked stakeholders to provide answers to 37 questions and considered all views presented. Whilst not every response we received for each individual question has been outlined in our summaries, we have considered and noted all responses during our analysis and response development. We

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recognise that some individual responses represent collective views, and we have considered this in our response and analysis. We have aimed, where possible and appropriate, to keep summaries succinct, aiding the readability and conciseness of the document.

### **Our Decision**

We have considered responses to the consultation and provided our response under individual chapters.

## 1. Fair Pricing Framework

### Section summary

In the previous consultation, we outlined draft guidance on how to interpret the fair pricing authorisation condition. The authorisation condition imposes the general obligation on authorised persons to provide prices that are fair and not disproportionate through an outcomes-based approach.

The draft guidance introduced a framework built around six key principles designed to achieve its overarching objective and deliver a set of six positive consumer outcomes, as well as one industry outcome. These principles were: cost reflectivity, cost efficiency, fair and reasonable returns, affordability, regulatory control, and price transparency. However, to avoid confusion and unintended consequences, we have updated the affordability principle, which is now called ‘consumer impact’.

The draft guidance sets out minimum expectations and, in some cases, examples of best practice for each principle, and explains how we would assess whether charges are fair and not disproportionate through the application of a fairness test.

Stakeholders generally supported the proposed regulatory approach and the high-level principles. However, many requested greater clarity in certain areas.

The following section summarises stakeholder responses by question and sets out our position in response.

### Question Analysis

Q1. Do you agree, partially agree, or disagree with the proposed guidance in relation to the cost-reflective principle?
Q2. Do you have any suggestions to improve guidance in relation to the cost-reflective principle?

Table 1: Response summary for consultation question 1

Response	Number	Percentage
Agree	14	37%
Partially agree	17	45%
Disagree	2	5%
No response	5	13%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

1.1 The majority of respondents either agreed or partially agreed with our proposal, with 32 leaving comments. Several participants welcomed the iterative approach, encouraging Ofgem to maintain ongoing engagement with the industry post go-

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live to support a deeper understanding of the market and to further enhance the guidance, particularly by incorporating relevant examples as they become available.

- 1.2 A few respondents thought that implementing cost-reflective pricing could increase bills for many customers, especially due to existing cross-subsidisation practices within the sector. Others thought costs should be transparent and broken down to ensure cost-reflectivity.
- 1.3 Several stakeholders requested greater clarity regarding which specific costs are deemed acceptable to pass on to customers, and sought further explanation on acceptable pricing methodologies under the cost-reflectivity principle. This was particularly relevant for smaller networks, not-for-profit organisations, those with hybrid ownership structures, as well as operators employing 'price promise' or counterfactual pricing strategies, and those setting prices at a portfolio level.
- 1.4 A minority of respondents wanted further clarification on the guidance's statement that 'consumers should pay for the additional costs they impose on the system', and one respondent felt the guidance was unclear about how cost-reflectiveness would be balanced with protections for affordability.
- 1.5 Some respondents argued that the guidance should do more to encourage the adoption of metering, given its potential to enhance efficiency, while others proposed minor, practical changes to the guidance, such as rephrasing certain sections for greater clarity and adding cross-references to related areas.
- 1.6 One respondent contended that meaningful implementation of cost-reflective pricing would not be achievable without changes to existing housing legislation and the introduction of new laws to permit varying existing leases, since costs are often included in service charges.

### **Ofgem response**

Respondents in general welcomed the iterative approach and encouraged continued engagement post go-live. We will continue to engage with stakeholders as the regime is implemented and will keep guidance under review, updating it where necessary to reflect market developments and feedback.

### **Price increases**

Regarding the concern around the cost-reflectivity principle resulting in increased prices in cases where an operator may be subsidising the network, we reiterate our position that the operator may still decide not to increase prices if they believe it benefits consumers and has clear rationale. We would not consider this, on its own, to breach the fair pricing principles. These principles should be considered in a manner consistent with the overarching objective and achieving the consumer outcomes. This may involve balancing different principles, such as (but not limited to) cost reflectivity and affordability, where appropriate.

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### Transparency

We agree that costs should be transparent and our guidance states that, in terms of best practice, we expect authorised persons to be transparent in cost reporting. Furthermore, guidance on what information should be provided to customers is included in the ‘billing and transparency’ guidance which is part of the wider consumer protections guidance (see related publication links on this document’s webpage). In addition to this, we are developing our pricing data reporting framework, including proposals to collect cost information such as operating expenditure from heat networks. Our consultation on regular data reporting draft guidance has recently closed and can be found [here](#).

### Clarity, metering and interdependencies

Some respondents requested further clarity on what the guidance meant by the statement that ‘consumers should pay for the additional costs they impose on the system’. Further information has been provided in the guidance, including further considerations about balancing cost-reflectiveness with affordability.

The fair pricing guidance does not impose an obligation to install meters. Currently, metering is regulated under the Heat Network (Metering and Billing) Regulations. New metering requirements will be set out in HNTAS. Therefore, we do not consider it necessary to provide additional guidance on metering beyond what was already included in the draft guidance.

We acknowledge that certain proposals in this framework have dependencies on the unbundling of individual heat charges from wider charges such as rent. For more information on these proposals please see [2025 ICP government response](#).

We have carefully considered the suggested small, practical changes to the guidance, and some have been incorporated.

Q3. Do you agree, partially agree, or disagree with the proposed guidance in relation to the cost efficiency principle?
Q4. Do you have suggestions to improve guidance in relation to the cost efficiency principle?

Table 2: Response summary for consultation question 3

Response	Number	Percentage
Agree	12	32%
Partially agree	19	50%
Disagree	1	3%
No response	6	16%

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*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

- 1.7 The majority of respondents agreed or partially agreed with our proposal, with 28 respondents providing comments.
- 1.8 Some respondents welcomed the iterative approach to developing the guidance and encouraged continued engagement with industry post go-live to deepen market understanding and enhance the guidance with more detail and best practice examples.
- 1.9 Several respondents raised a lack of incentive mechanism to drive efficiency. They argued that this could increase prices and make the sector less attractive to invest, and that financial incentives in the form of retention of some efficiency savings via increased profits should be allowed.
- 1.10 Some stakeholders raised concerns of potential conflict or overlap with HNTAS and urged Ofgem to ensure this does not happen. Some suggested that HNTAS compliance should provide assurance that sufficient investment in technical efficiency has been made. One respondent proposed that future guidance should explain interactions between the Fair Pricing Framework, HNTAS, and housing law in relation to cost efficiency.
- 1.11 Some respondents noted that achieving efficiency requires significant capital investment and might result in higher costs in the short and medium term. A few sought further clarity in relation to the funding required, for example:
  - whether it would be appropriate for heat suppliers to raise improvement funds, for example, as part of a long-term plan
  - whether this could be done through the heat tariff
  - whether this capital should come from tariff or service charges, noting that there are distributional impacts to be considered
- 1.12 Some respondents sought further clarity on how efficiency will be assessed in practice, with a minority raising concerns about measuring efficiency by comparison given networks' different characteristics. Suggestions included providing examples about acceptable evidence of efficiency, such as:
  - benchmarking against similar networks demonstrating competitive procurement
  - showing year-on-year performance improvements
  - worked examples showing efficient management for different network sizes

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- efficiency expectations should be flexible and relative to factors such as scale, technical legacy and age of the network

1.13 One respondent said that social landlords are bound by procurement regulations and value-for-money tests under the [Public Contracts Regulations 2015](#) and the [Regulator of Social Housing's Value for Money Standard](#), and that we should acknowledge compliance with these regimes as evidence of efficient procurement. They also thought that the guidance should recognise the [Landlord and Tenant Act 1985](#) (sections 18 -30) as an existing framework for assessing cost reasonableness.

1.14 Some respondents sought greater clarity on efficient procurement practices. They asked for assurance that selecting options other than the lowest-cost bid can be justified where this delivers better outcomes and noted that exceptions to market-testing may be appropriate where only one provider can realistically compete, consistent with public procurement rules. Some respondents highlighted the use of portfolio-level framework agreements, arguing these can deliver value for money through volume discounts and reduce the relevance of network-level assessments. They requested confirmation that such approaches are legitimate. One respondent also raised concerns about procurement constraints arising from housing legislation, such as consultation requirements, and asked that these be acknowledged.

1.15 One respondent sought to clarify how we will treat higher costs arising from decarbonisation upgrades or compliance investment which are not inefficiencies but essential obligations under the [Energy Act 2023](#).

1.16 Respondents proposed several improvements to the guidance. Suggestions included minor wording changes to ensure neutrality, and additions to the guidance to improve cost-efficiency beyond focusing on current performance, such as:

- promoting forward planning
- encouraging periodic market testing to assess outsourcing versus in-house delivery
- encouraging continuous improvement through collaborative purchasing

### Ofgem response

We note the feedback regarding the absence of a defined incentive mechanism to drive efficiency. We are not establishing a price control process, so we do not consider it appropriate to introduce a formal incentive framework. However, we agree with the principle that operators should be able to retain some efficiency savings in the form of profit. Our fair pricing principles are not prescriptive and provide the flexibility for

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increased profit to be made, for example in cases of exceptional performance. Further detail has been included in the guidance to make this point clearer.

### **Technical and cost efficiency**

For detailed technical standards and best practices, we refer to the HNTAS, which is being jointly developed by DESNZ and the Scottish Government. Once HNTAS requirements are further defined, we may review our guidance to enhance clarity if needed.

It is worth clarifying that, whilst the fair pricing principles introduce a general expectation that heat networks should operate efficiently, we will not be setting the level of technical efficiency standards under the fair pricing framework, as this is the role of the forthcoming HNTAS. We will not consider efficiency in isolation but alongside other factors such as prices, profit, and relevant network characteristics. Guidance has been amended to make this point clearer.

Furthermore, we acknowledge that different heat networks will have varying levels of technical efficiency, which may result in legitimate differences in pricing. The guidance makes it clear that these factors will be considered when assessing whether prices are fair and proportionate, to ensure fair comparisons.

We acknowledge the feedback that achieving efficiency may require significant capital investment, which could lead to higher costs in the short and medium term. We expect operators to plan improvements in a way that balances the need to achieve efficiencies and long-term sustainability with the principle of affordability.

This can be achieved by, for example, planning, adopting a long-term approach, and considering making incremental improvements where possible and beneficial. The guidance does not prescribe how improvement funds should be raised. In relation to the use of service charges to recover heat network costs, we refer to our policy on unbundling charges (pg. 88 [Heat networks regulation: implementing consumer protections - Government response](#)).

### **Compliance with existing regulations**

We note the suggestion that the guidance should recognise compliance with existing regulation as evidence of efficiency or cost reasonableness. Whilst we acknowledge that these frameworks may include value-for-money considerations and apply to certain heat networks, we expect authorised entities to take responsibility for ensuring compliance with all relevant legislation within their scope. In principle, compliance with other regimes does not remove the need to follow this sector-specific guidance, although it may be a factor we consider when assessing whether prices are fair and not disproportionate. However, if issues between the application of our guidance and other existing regulations arise these will be considered on a case-by-case basis.

On the allowance for recovery of costs necessary for compliance with existing legislation, the framework does not intend to stop the recovery of legitimate costs.

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However, as mentioned above, measures to minimise the impact on consumers' bills, such as good planning and incremental upgrades where possible and beneficial, are encouraged.

### Clarity

Regarding the feedback from stakeholders seeking greater clarity on efficient procurement practices, the guidance sets out expectations of what best practice looks like, but it is not prescriptive. We acknowledge that portfolio-level framework agreements can, in principle, deliver value for money through economies of scale and volume discounts. Generally, heat networks are expected to be able to justify their procurement approach and demonstrate how it aligns with the fair pricing high-level objective, principles, and consumer outcomes.

We have carefully considered the proposed improvements to the guidance. Some of these suggestions have been incorporated into the final version, including changes that strengthen clarity and support good practice.

Q5. Do you agree, partially agree, or disagree with the proposed guidance in relation to the fair and reasonable returns principle?
Q6. Do you have suggestions to improve guidance in relation to the 'fair and reasonable returns' principle?

Table 3: Response summary for consultation question 5

Response	Number	Percentage
Agree	6	16%
Partially agree	17	45%
Disagree	11	29%
No response	4	10%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

- 1.17 A majority of respondents agreed or partially agreed with our proposals and 34 respondents provided comments.
- 1.18 A minority of respondents said that this area could be developed further in future iterations of guidance to gain understanding of investment risk and investment performance, so judgement can be sufficiently informed when deciding a fair and reasonable rate of return.
- 1.19 15 respondents raised concerns that the guidance provides insufficient detail on what constitutes an acceptable level of return in practice, or on how this would be

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assessed. Respondents typically argued that sufficient clarity on this is needed to give investors the confidence to commit capital. Others had concerns that the guidance might not provide sufficient protection to consumers. Whilst there is consensus among these respondents that further clarity is needed, some agreed with our current approach of not setting specific levels, and others favoured greater definition. Proposals to address these concerns included:

- a notional upper limit
- providing indicative reference points such as typical range of returns
- further clarity, including examples, on how we would evaluate and compare returns
- providing reassurance that an acceptable level of return will be understood in the context of achieving a sufficient return on capital
- providing further clarity on how this provision aligns with the forthcoming heat network zoning legislation
- providing clearer guidance on how government funding should be reflected in pricing and margin calculations

1.20 Some respondents said that returns should be assessed over the long term, not on a single year basis. They argued that heat networks have long investment cycles, and returns naturally vary year-on-year depending on investment requirements and operational performance.

1.21 Several respondents said that the guidance should be updated to reflect the reality of not-for-profit networks. Respondents proposed:

- ensuring the principle is compatible with the regulatory obligations placed on housing providers, notably the Landlord and Tenant Act obligations.
- defining not-for-profit
- acknowledging reinvestment models, where returns are reinvested into services and resident support, not distributed as profit

1.22 One respondent requested further clarification on how returns are assessed for organisations with management responsibilities under lease agreements, noting that energy management costs and profits may be intertwined with the cost and profit related to delivering other services.

1.23 Some respondents thought that if customers are being charged proportionately, the profitability of the network should not be relevant on its own.

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- 1.24 A minority of respondents argued that our current proposal introduces an effective profit cap through principles, as the guidance implies there is a profit level above which profit is deemed to be unfair, which can deter investment into the sector.
- 1.25 One respondent disagreed with the proposal to monitor profit levels, arguing that we should not investigate cases where profit levels were higher than what we would expect, given the lack of clarity around what is considered 'fair and reasonable'. Furthermore, they said that monitoring would send a strong signal to investors that this is the first step towards full price and profit regulation without due regard to level of risk. They further argued that we do not regulate profit in gas and electricity markets, but return on investment. Finally, they stated that networks should be able to earn a fair and reasonable return that reflects the risks faced by them, and this should be led by the market and not the regulator. To protect consumers, they proposed a tariff cap based on external benchmarking approach.
- 1.26 One respondent said that capping profits at the 'risk associated with the investment level' would reduce incentives to increase efficiencies.
- 1.27 One respondent proposed to strengthen the principle by publishing analytical tools for assessing returns, requiring disclosure of capital and financing, and mandating clearer reporting of profitability drivers. Where operators claim exceptional performance to justify higher returns, those claims must be evidenced by consumer outcomes.

### **Ofgem response**

We note the feedback requesting greater clarity on what constitutes an acceptable level of return. We also note that a minority of respondents disagreed with the inclusion of profit considerations in the pricing framework.

### **Regulatory approach**

Profit is a key factor in pricing under monopoly, and as such, we believe consideration of profits needs to be included in any pricing framework. As a heat network customer does not have the option to change supplier or operator and face high financial and practical barriers to disconnect from their heat network supplier, there is minimal competitive pressure. Without regulation, heat networks could raise prices by increasing profits above what would be expected in a competitive market, which would harm consumers. Though we believe it is important to consider profit as part of our principles-based approach, we are not introducing direct regulation of profits or returns on investment.

Our principles-based approach to regulation seeks to ensure both investor confidence and consumer protection, while maintaining flexibility to reflect the diverse circumstances of heat networks. This approach means the guidance remains high-level, and it does not set specific profit levels. Instead, heat networks are expected to

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have regard to the principle that profits should be fair and reasonable in relation to risks and performance.

We recognise that heat networks are capital intensive and have their own risk versus reward profile. Profit levels will also vary based on factors such as performance, ownership model, and market conditions over time. The guidance makes clear that we support networks earning a fair return that reflects these considerations.

We will monitor profitability across the sector to better understand the market and the drivers behind pricing decisions. However, we acknowledge the challenges and limitations of monitoring profits, as data may be limited and higher profitability does not necessarily indicate disproportionate pricing.

This approach allows us to take account of the complexity and variability across projects, rather than applying a one-size-fits-all limit. It also ensures that returns are understood in the context of achieving a sufficient return on capital, while protecting consumers from unfair and disproportionate charges.

In addition to the above, we believe that providing estimates without good data would not be appropriate and would risk sending the wrong signals to the market.

We agree in principle that the timing of returns is an important consideration when looking at profits, given the long-term nature of heat network investments. We will explore how best to incorporate this into our methodology.

### **Industry outcome**

We have updated the ‘industry outcome’ in the guidance to make clear that sector growth is a desired outcome of this framework, and that a fair return for investors is a key element of achieving this, alongside ensuring consumers have confidence in the sector through fair pricing.

### **Not-for-profit networks**

Some respondents suggested that the guidance should be updated to reflect the reality of not-for-profit networks. The guidance recognises that the fair and reasonable returns principle is not relevant for authorised persons operating under a purely cost recovery model, as defined in Table 2 within the fair pricing guidance. At the same time, the guidance is intended to be high-level and flexible enough to apply to networks that do not follow a strictly cost recovery approach, for example, where returns are reinvested into other services or resident support. For more detailed discussion on the relevance of profitability assessments for not-for-profit networks please see ‘chapter 4. Profitability analysis’ of the [2025 fair pricing response](#).

### **Existing legislation**

The guidance does not override any existing legislation, including obligations under the [Landlord and Tenant Act](#). We do not consider that a formal definition of ‘not-for-profit’ is required for the first iteration of the guidance, as these are not categories used for

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market segmentation. However, we will take the individual circumstances of networks into account when considering compliance and enforcement.

### Other comments

In relation to the proposal to introduce a tariff cap based on an external benchmark as an alternative to including profit within the framework, we maintain our position not to include such a tariff cap, as set out in our previous response document. Given the diversity of the market, a single counterfactual based on alternative heat sources is unlikely to reflect competitive prices for many networks, particularly over time. This approach risks networks pricing above a more competitive level. However, we do intend to use external benchmarks as part of our benchmarking methodology.

Q7. Do you agree, partially agree, or disagree with the proposed guidance in relation to the affordability principle?
Q8. Do you have suggestions to improve guidance in relation to the affordability principle?

Table 4: Response summary for consultation question 7

Response	Number	Percentage
Agree	14	37%
Partially agree	14	37%
Disagree	4	10%
No response	6	16%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

1.28 This question was generally supported by respondents with 74% in full or partial agreement with the proposed guidance in relation to the affordability principle. Stakeholders generally supported the inclusion of affordability as a core principle, highlighting its role in protecting consumers, particularly those in vulnerable situations. Respondents emphasised that prioritising affordability could help safeguard against excessive costs and bolster consumer confidence in the sector.

1.29 A minority of stakeholders questioned whether a separate affordability principle added value and argued that it introduces subjectivity and greater uncertainty for potential investors. They recommended that Ofgem focus on enforcing the existing core principles and consider affordability as part of the overall consumer outcomes.

1.30 A few responses requested more clarity on the definition of affordability, with stakeholders emphasising the need for a clear and measurable methodology. One

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respondent suggested that affordability should be based on income levels, specific energy needs (including health-related requirements), and differences in regional costs. Many respondents expressed a desire for further operational guidance and best practice examples, particularly in relation to debt management, back-billing, cost passthroughs and shock bills.

- 1.31 Some stakeholders noted that the guidance does not adequately address the potential conflict between the affordability principle and other core principles, such as cost reflectivity. They highlighted a scenario where a network's genuine costs result in charges that are deemed unaffordable and questioned what the resolution would be.
- 1.32 Many stakeholders raised the topic of cross-subsidisation, expressing that the proposed guidance could benefit from greater clarity on what would be acceptable and how it would be determined whether consumers faced 'disproportionate prices' as a result. Many respondents advocated for guidance and examples that include real-world scenarios illustrating best practices and circumstances where cross-subsidisation would not be accepted. On a similar topic, some respondents also requested further clarity on the acceptance of portfolio-level pricing, particularly where organisations manage networks with varying levels of technical efficiency and/or underlying costs, which may have the interpreted effect of resulting in 'disproportionate pricing'.
- 1.33 Other general recommendations and improvements suggested by respondents included adapting and extending existing fuel poverty schemes and financial assistance programmes, such as the Warm Home Discount and Winter Fuel Payment, to better support heat network customers. Clear explanations and worked examples of how affordability interacts with housing law. Guidance on how operators should evidence the consideration of affordability in tariff decisions.

### Ofgem response

We welcome the broad support from stakeholders on the proposed guidance in relation to the affordability principle, echoing our views that having regard to affordability is particularly important for the protection of consumers in vulnerable situations. We note, however, that some confusion about the scope and objective of this principle remained.

This is in part due to the term 'affordability' being interpreted differently by different stakeholders, raising significant concerns that the principle would be misinterpreted in future. In light of these considerations, we have decided to update this principle and rename it 'consumer impact'. These changes better reflect the intended purpose and content of the principle and helps distinguish it from wider policy discussions on individual consumer affordability. Importantly, the underlying principle and the areas it covered remain the same, and authorised persons are still expected to have regard to consumers' benefit and best interests as previously proposed.

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### Affordability principle

On the need for an ‘affordability’ principle, in the [2025 fair pricing consultation](#) and [2025 fair pricing response](#) we clarified that this principle is in relation to what is within the control of heat networks, such as reducing the likelihood and impact of shock bills. While some of these measures will be covered under principles such as cost efficiency, not all measures, such as reducing the impact of shock bills, would fit under other principles.

### Clarity, definitions and guidance

Some respondents requested more clarity on the definition of affordability. We recognise that a clear understanding of affordability is essential to ensure authorised persons are able to implement the principle effectively. We also recognise some aspects of affordability will be partly beyond the control of heat networks, such as high wholesale energy prices. In our draft guidance, we outline that affordability relates to ensuring that charges for heat are fair and reasonable, considering what is within the control of heat networks. This involves practices such as taking steps to minimise the likelihood and impact of shock bills, and ensuring that payment terms and support arrangements are in place for those who may struggle to pay. While some aspects of affordability are addressed under other principles such as cost efficiency, the affordability principle specifically focuses on the consumer’s ability to pay, particularly for those in vulnerable circumstances. This is complementary and consistent with guidance around those in payment difficulty and the vulnerability protections.

Stakeholders also expressed interest in operational guidance and practical examples around several affordability related topics such as debt management, back-billing, cost passthroughs, shock-bills and cross subsidisation. At this stage, we will not be able to provide further operational guidance, in the form of templates and examples within the first iteration of guidance. As regulation commences and we obtain further information and data from the market, we will evaluate our existing guidance and consider the development of supportive tools such as templates and practical examples.

### Conflict between principles

Respondents raised the potential conflict between the affordability principle and other core principles. We recognise that, in practice, there may be occasions where the affordability principle, now known as the consumer impact principle, may be in tension with other core principles, such as cost-reflectivity. Our proposed approach, as set out in the [2025 fair pricing draft guidance](#) and our [2025 fair pricing response](#), is that these principles should be considered in a manner consistent with the overarching framework objective. This may involve balancing different principles where appropriate such that it yields the most favourable outcome for consumers.

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Q9. Do you agree, partially agree, or disagree with the proposed guidance in relation to the regulatory control principle?

Q10. Do you have suggestions to improve guidance in relation to the regulatory control principle?

Table 5: Response summary for consultation question 9

Response	Number	Percentage
Agree	19	50%
Partially agree	9	24%
Disagree	1	3%
No response	9	24%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

1.34 Stakeholders displayed general support for the proposed guidance in relation to the regulatory control principle, with 74% of respondents fully or partially agreeing. Most respondents recognised the importance of regulatory control in ensuring fairness, transparency and accountability in heat network pricing. They emphasised that the principle is an important inclusion within the pricing framework.

1.35 The most common theme amongst respondents to this question was the need for greater clarity in guidance regarding specific sections of the market and recommendations on useful additions to further support heat networks in complying with the regulatory framework.

1.36 One respondent requested clarity on expectations of not-for-profit providers within the framework. They highlighted the need for Ofgem to tailor compliance pathways to reflect the financial models and resident demographics of social housing schemes. Another respondent suggested that the guidance should clarify that the guidelines are limited to services related to delivering regulated services, as opposed to wider supply chains necessary for running a business but not connected to the regulated service.

1.37 Several stakeholders raised the topic of examples and standardised templates in relation to this principle's guidance. They recommended that guidance could benefit from the inclusion of practical examples, such as detailed tendering criteria to assess contractors' ability to understand and comply with regulatory obligations as well as guidance on checks that networks can employ to ensure compliance.

1.38 Some respondents raised points related to the consideration of legacy and pre-existing contracts at the point of regulatory commencement. One respondent

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questioned Ofgem's consideration of the period between guidance publication and subsequent enforcement of the Authorisation Conditions (ACs), whilst another respondent recommended the inclusion of a 'transition period' within the principle that would allow suppliers to make necessary adjustments to contracts at more appropriate and natural times. They cited the approach outlined in paragraph 5.19 of the guidance on consumer protection as a precedent.

### **Ofgem response**

We welcome the support for the proposed guidance on the regulatory control principle and the acknowledgement that the principle is an important component of the fair pricing framework in ensuring fairness, transparency, and accountability.

### **Guidance clarification**

One respondent considered that we should be clear that the guidance is limited to the delivery of regulated services and not to the wider supply chain. We appreciate the need for clarification on this and have amended the wording of the principle's definition in the guidance to reflect this.

Several stakeholders questioned the treatment of legacy contracts at the point of regulatory commencement. We are aligned with the consumer protection guidance in that we do not expect existing contracts to be changed by the date of regulatory commencement. We would expect suppliers to make necessary changes to supply contracts at a time when it is natural to do so.

For more information on how legacy arrangements are treated in the framework, please refer to the legacy arrangement subsection of the cost allocation guidance.

### **Templates and examples**

At this stage we are unable to provide standardised templates and examples in the first iteration of guidance. As regulation commences and we obtain further information and data from the market, we will evaluate our existing guidance and consider the development of supportive tools such as templates and practical examples.

<p>Q11. Do you agree, partially agree, or disagree with the proposed guidance in relation to the price transparency principle?</p> <p>Q12. Do you have suggestions to improve guidance in relation to the price transparency principle?</p>
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Table 6: Response summary for consultation question 11

<b>Response</b>	<b>Number</b>	<b>Percentage</b>
Agree	14	37%

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Partially agree	10	26%
Disagree	8	21%
No response	6	16%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

- 1.39 The respondents broadly agreed with the proposed guidance in relation to the price transparency principle and 28 respondents provided comments.
- 1.40 Among the respondents who agreed, a minority expressed explicit support for clear and accessible communication of prices. Alternative formats for digitally excluded consumers were requested.
- 1.41 Respondents raised concerns that overly technical disclosures or comparisons could mislead consumers and trigger complaints. It was stressed that simplicity and context should be prioritised.
- 1.42 Several respondents requested the provision of materials enhancing price transparency, such as standardised tariff formats, examples and templates for billing to ensure consistency and clarity. It was suggested that a standard tariff disclosure template showing information such as fixed and variable charge components, cost breakdowns and other costs included in tariffs, can be provided for consistent comparison between heat networks. Guidance could also specify the minimum level of information.
- 1.43 Some respondents requested further details and descriptions on best practices and the level of detail required to meet transparency standards set out in the principle.
- 1.44 One respondent suggested that pre-contractual transparency should be covered in the guidance as an additional consumer outcome: ‘consumers are able to make informed choices before buying or renting a heat network property.’
- 1.45 A minority of respondents urged that market diversity should be recognised explicitly in the guidance in relation to price transparency. They mentioned the need for flexibility and that expectations should be set out for different groups, such as unmetered properties and shared ground loop (SGL) networks with simple charge structures.
- 1.46 A few respondents emphasised the need to align guidance with existing housing legislation (such as the [Landlord and Tenant Act 1985](#)), particularly for social landlords, to avoid duplication or inconsistency. They queried on how the transparency obligations would interact with existing housing regulations and service charge frameworks.

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### **Ofgem response**

We welcome the broad support for the price transparency principle.

### **Importance of balance and context**

We agree that transparency must be meaningful and accessible to consumers, and not overly technical or burdensome. As set out in both our consumer protection and fair pricing protection guidance and response, our aim is to ensure consumers can understand their charges and have confidence that they are fair. We recognise the need to balance information and clarity with simplicity. We will develop central price transparency proposals alongside billing transparency. We will also develop supporting materials for consumers to achieve this balance. Future work will include undertaking further engagement and research to ensure that the proposals are effective in practice and deliver clear value to consumers.

### **Demand for more details, examples and best practice**

We are considering the suggestion to include standardised formats and templates to support consistent and clear communication of tariffs, for example this involves:

- heat network entities presenting billing information to customers: billing transparency proposals
- heat network entities reporting pricing information to Ofgem: basic pricing data from heat network entities through regular data reporting via a digital platform (see [regular data reporting draft guidance](#) for details)
- Ofgem presenting pricing information to consumers: further engagement and research with consumers shaping the central transparency proposals

In parallel to the billing transparency proposals, we will continue to explore ways to move towards more standardised tariff reporting (see [regular data reporting draft guidance](#) for details), and subsequently the disclosure of this information centrally.

### **Expectation on unmetered and SGL**

We acknowledge the diversity of heat networks and agree that expectations should be proportionate. It is our intention that the data reporting journey and publication of data under central price transparency will cater for networks with simpler charge structures such as unmetered properties and SGL networks while meeting transparency expectations.

### **Pre-contractual transparency**

As highlighted in our [consumer protection response](#), consumers should be able to make informed choices before entering into agreements. We will keep the guidance under review depending on any future work on pre-contractual transparency.

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### Interaction with housing regulations and existing protections

We recognise the importance of aligning our guidance with existing housing legislation, including the [Landlord and Tenant Act 1985](#). We are engaging with MHCLG and DESNZ to explore this interaction further. Future iterations of guidance will clarify how transparency obligations relate to service charge frameworks and will aim to avoid duplication or inconsistency.

Q13. Do you agree, partially agree, or disagree with the proposed ‘fairness test’?
Q14. Do you have suggestions to improve guidance in relation to the ‘fairness test’?

Table 7: Response summary for consultation question 13

Response	Number	Percentage
Agree	11	29%
Partially agree	14	37%
Disagree	5	13%
No response	8	21%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

- 1.47 The respondents broadly agreed with the proposed guidance in relation to fairness test and 30 respondents provided comments.
- 1.48 Some respondents questioned whether statistical and economic models can yield objective and robust results given market diversity and current data gaps. Several asked Ofgem to collect more data and market intelligence to prove the objectivity and effectiveness of the tools before application. Data collection of at least two years was suggested.
- 1.49 Several respondents asked for worked examples and practical case studies showing how the test will be applied including data collection, analysis, and decisions under the test across different network groups, in current or future iterations of this guidance.
- 1.50 Some respondents requested clearer definitions of ‘fair’, ‘disproportionate’, and ‘reasonable’, or indicative benchmarks and thresholds to reduce disputes. Some respondents expressed concerns that the lack of clarity and high-level guidance that is open to interpretation would become a source of disputes and administrative burden.
- 1.51 Several respondents also asked how the test will treat different market segments or groups and whether it will apply to legacy contracts. Examples of

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these groups include for-profit and not-for-profit networks, new and legacy networks with limited historical data, large urban schemes and small networks.

1.52 Several respondents provided suggestions for improving the guidance, including setting indicative thresholds on disproportionate pricing. A minority of respondents suggested a structured framework to guide case-by-case assessment with clear procedures for resolving disputes on fairness test, and with defined roles for Ofgem, ombudsman and other bodies, should be set out. It was suggested that:

- Ofgem should set out what constitute sufficient evidence for each criterion in the fairness test
- the inclusion of details on how Ofgem will approach the fairness test during the period where the relevant statistical and economic models referenced are still under development

1.53 One respondent stated that it is important for the guidance to set out the details of 'best practice in economic regulation' mentioned in paragraph 1.53 of the [2025 fair pricing guidance consultation](#) as raised by respondents in the earlier consultation.

1.54 A few respondents were concerned that a subjective or opaque test could increase the risks of inconsistent enforcement, create significant risks for investors (risk of ex-post profit clawback), and deter investment. It was also mentioned that applying the test to many standalone networks could become onerous. Some respondents reiterated their suggestion of relying solely on external benchmark to screen for further investigations.

1.55 A few respondents challenged test questions including 'is the tariff prohibitive to uptake?' in the test and questioned how it is measured, arguing it conflates decarbonisation objectives with fairness and may misidentify legitimate cost-reflective tariffs as unfair.

1.56 A minority of respondents support prioritising cases that affect consumers in vulnerable circumstances for actions within the fairness test's prioritisation process. They also recommended more explicit considerations to impacts on vulnerable customers in the framework.

1.57 A minority of respondents asked for proportionality and presumed compliance where existing housing legislations such as the leasehold system already constrain pricing.

### Ofgem response

We welcome the broad support for the proposed guidance on the fairness test and the acknowledgment of its importance in administering the fair pricing framework.

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### **Importance of robust and transparent models**

We acknowledge stakeholder concerns about the robustness of statistical and economic models used to assess fairness. As set out in our [fair pricing consultation response](#), we will continue to develop benchmarking and profitability assessment tools, informed by best practice in economic regulation. We agree that further data collection and continuous engagement with different parties including stakeholders and specialists are needed in the process of operationalising the fairness test and developing these assessment tools, and we will take a phased approach to implementation. This guidance will be kept under review and updated in the process.

### **Data requirements**

We agree that reliable data and market intelligence are essential for operationalising and applying the fairness test effectively, and that a certain amount of data will be required for the analysis. Nevertheless, we intend to develop our analysis iteratively based on available data, rather than starting the analysis after collecting perfect data. Please refer to our [regular data reporting draft guidance consultation](#) detailing ongoing reporting requirements.

### **Demand for clear definitions, case studies and best practice**

Whilst we are not defining terms such as 'fair' and 'not disproportionate', we have outlined how we will apply these concepts when implementing the fair pricing framework. At this stage, we are unable to provide worked examples and case studies to illustrate how the fairness test will be applied across different network types, as the analytical tools and procedures are still under development and will evolve as more data becomes available. We would also like to reiterate that our approach intends to be principle-based and flexible, meaning that it would be inappropriate to provide indicative benchmarks or thresholds as this would risk these being interpreted as binding, making these levels prescriptive in effect. It is our intention that the analytical tools under development will take different network types into account. This guidance will be kept under review and updated in the process.

### **Clear roles, process and dispute procedures, transition to more developed methods**

We agree that details of price investigation (which is out of scope of this consultation) including the roles of Ofgem, ombudsman, and other bodies, and the transition to more developed methods should be clearly defined and laid out. Please refer to the price investigation chapter in our fair pricing consultation and future consultation on price investigation. Note that the fairness test (which is distinct from price investigation) sets out, at a high level, how we would look to apply the fair pricing authorisation condition and principles effectively and consistently to identify potential cases of disproportionate pricing. It outlines the type of questions we might consider and how tools such as benchmarking could be applied. Where prices for consumers appear to be disproportionate, for example through the outcomes of the fairness test, we will

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have the power to investigate. As noted above, for more detail on price investigations, please refer to the price investigation chapter in our [fair pricing consultation](#) and our future consultation on price investigation. We will also consider providing examples of evidence for each criterion in the test in future iterations of the guidance.

### **Segmentation**

We recognise the need to tailor the fairness test to different market segments. Heat networks are required to indicate and update their pricing methodology as part of data reporting (see [regular data reporting draft guidance](#) for details) to provide contextual information for interpreting their prices. For example, networks that are charging to recover their costs only should report as ‘purely cost recovery’, and networks with legacy contracts should report this status as part of their pricing methodology. We will ensure that assessments are proportionate and reflect the key characteristics of each segment. For networks with limited historical data, we would like to clarify that we would not collect pricing data from before authorisation conditions are introduced. Please see [regular data reporting draft guidance](#) for more information. For other data submissions, please refer to [registration guidance](#) and forthcoming HNTAS requirements respectively.

### **Investment uncertainty and incentives**

We understand concerns about the potential impact of the fairness test on investment. It is our intention that the test is applied transparently and consistently to avoid creating uncertainty or deterring investment, as is reflected in the inclusion of the heat network uptake consideration. Details of the tools used in the fairness test will be subject to future consultation to increase transparency and reduce uncertainty. We will continue to engage with stakeholders as the regime is implemented and will keep guidance under review, updating it where necessary to reflect market developments and feedback. We also believe that our proposed way of prioritising actions is able to reduce the burden on standalone networks.

### **Disagreement on prohibitive to heat network uptake question**

We note the concerns about including ‘is the tariff prohibitive to uptake?’ in the fairness test. We would like to clarify that fairness test is not only about identifying potential disproportionate pricing, and that this question is not primarily for identification of potential disproportionate pricing. This question is intended as an example of the types of considerations that help inform our understanding of pricing in the sector, based on broader policy outcomes as well as the pricing principles. Our view is that it is important to ensure that heat networks’ behaviour and the general outcomes of the fairness test align with the fair pricing principles and broader policy goals. We will ensure that the test will apply to cost-reflective tariffs appropriately.

### **More emphasis on vulnerable customers**

We agree that impacts on vulnerable consumers should be explicitly considered in the fairness test. As set out in our consumer protection proposals, we will ensure that the

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framework supports equitable outcomes. Impacts on vulnerable consumers, along with other factors set out in the appendix as examples, will be taken into consideration. We have amended the appendix on the fairness test in the guidance to emphasise this.

### Interaction with housing regulations

We acknowledge that some legal frameworks may already constrain pricing. As we said in our response to questions 2 and 3 above, we expect authorised entities to take responsibility for ensuring compliance with all relevant legislation within their scope. In principle, compliance with other regimes does not remove the need to follow this sector-specific guidance, although it may be a factor we consider when assessing whether prices are fair and not disproportionate. However, if issues between the application of our guidance and other existing regulations arise these will be considered on a case-by-case basis.

Q15. Do you agree, partially agree, or disagree with the proposed market segmentation approach?
Q16. Do you have suggestions to improve the proposed segmentation approach?

Table 8: Response summary for consultation question 15

Response	Number	Percentage
Agree	7	18%
Partially agree	16	42%
Disagree	5	13%
No response	10	26%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

1.58 This question obtained general support from respondents with 60% in full or partial agreement with the proposed market segmentation approach as a way to tailor regulation proportionately and reflect the sector's diversity. Some respondents also welcomed the expansion of segmentation categories to include more specific approaches to pricing methodology. The majority of respondents that voiced support also put forward caveats and considerations regarding the segmentation approach.

1.59 A common point raised by many respondents was the risk of oversimplifying the complexity of the heat networks sector with the current segmentation approach. Respondents emphasised that the proposals do not sufficiently account for variations in metering arrangements, tenure types, operational models, and

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regional differences. Conversely, a minority of respondents suggested simplifying and tightening the segmentation approach, permitting well-justified exemptions only for small and not-for-profit schemes.

- 1.60 Several stakeholders requested for clearer definitions for terms such as 'not-for-profit' and 'small operator' and for further guidance on how networks operate under mixed models (such as for-profit operators managing not-for-profit networks) would be treated. Respondents recommended that Ofgem use sector-specific precedents as useful guidance when clarifying definitions. One respondent stated that it would be beneficial to obtain further clarity and guidance on how prices set under different methodologies would be tested and compared.
- 1.61 Some respondents questioned the appropriateness of vulnerability as a segmentation characteristic. They stated that the guidance does not specify what proportion of vulnerable consumers would trigger this segment classification and how this would be applied in practice. They also argued that vulnerability is not a structural or technical feature of the network and is therefore not a distinct segment. These respondents believed that vulnerability would be better addressed through wider components of the regulatory framework such as consumer protection standards, affordability measures' and debt management guidance.
- 1.62 A minority of stakeholders raised the circumstance of heat charges bundled with rent and service charge as an important segment. One of these respondents noted that the current guidance treats the bundling of heat charges with rent and with service charges as interchangeable. However, in practice, the legal rights and obligations of heat operators and suppliers, who are also landlords, can differ significantly between these arrangements. They called for Ofgem to develop a more detailed and differentiated approach.
- 1.63 A few stakeholders advocated for a more illustrative and accessible guidance around segmentation, making it easier for consumers to understand their rights and protections within the heat network sector. One respondent suggested the use of interactive tools such as flowcharts and decision trees to reflect the sector's complexity, whilst another emphasised the importance of simplifying guidance to ensure consumers feels informed and empowered to advocate for quality service. Another respondent requested the use of detailed examples showing how different types of networks are categorised and how segmentation affects compliance, enforcement, and pricing.
- 1.64 Some respondents highlighted the need for more detailed guidance on unmetered heat networks, particularly given that nearly 60% of heat network consumers currently lack individual meters and the lead time before widespread meter installation under HNTAS. They recommended that Ofgem develop clear distinctions in regulatory approach between metered and unmetered networks,

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including differences in cost reflectivity and affordability guidance for prepayment versus credit meters. One stakeholder raised concerns regarding SGL arrays, which are inherently unmetered since consumers pay their energy supplier directly for the electricity powering their heat pumps. They argued it would be inappropriate to require SGL array owners to estimate unmetered usage, as these would effectively be zero.

1.65 A minority of respondents made suggestions for additional segments to be added to the framework. Two respondents advocated for bulk supply as a distinct segment, recognising that additional cost drivers and tariff-setting roles exist beyond the bulk supply boundary, and that bulk suppliers should only be held responsible for factors within their control. One respondent proposed that heat networks operated by a single organisation, such as a university campus, should be identified as a separate category due to a different supplier-consumer relationship. Another respondent recommended that the segmentation framework more clearly distinguish between district and communal heat networks.

### **Ofgem response**

We welcome the broad support from stakeholders regarding the proposed updated segmentation approach, including the addition of segments based on pricing methodologies in the sector, recognising the value of tailoring regulation to reflect the sector's diversity. Our aim is to ensure that the segmentation approach is sufficiently flexible to accommodate the varied operational and physical characteristics present across networks in the sector.

### **Definitions**

Some respondents requested definitions for terms such as 'not-for-profit' and 'small operator'. At this stage, we do not believe a formal definition of 'not-for-profit' nor one of 'small heat networks' is required for the application of the proposed first guidance iteration, as these are not categories used for market segmentation, though the individual circumstances of networks will be taken into account when considering compliance and any potential enforcement.

### **Vulnerability**

Stakeholders questioned the inclusion of vulnerability as a segment and the threshold that would classify networks within it. In the draft guidance, we explained that the level of vulnerability might be a factor when prioritising regulatory actions. While vulnerability was shown in the segmentation table, we noted that it was not strictly a matter of market segmentation. To avoid confusion and any impression that we are creating a dedicated 'vulnerability segment', we have removed vulnerability from the segmentation table. However, the guidance still states that vulnerability may be considered when prioritising regulatory actions.

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### List of segments

A few respondents stated that the proposed approach does not sufficiently account for the variations between networks in the sector. We acknowledge the diversity of the heat network market and the need for our regulatory approach to be proportionate to different types of networks. In the [2025 fair pricing consultation](#), we explored a long list of network characteristics and possible segments. For this iteration of guidance, we have taken a more focused approach, identifying the segments that would require a differing approach to the guidelines.

Respondents gave suggestions for additional segments to be added to the table in guidance. We believe these additional segments, whilst valid characteristics of networks, will not require a substantially different treatment of the guidance in order to comply with the framework. It is also worth noting that in our case-by-case approach to pricing investigations, individual characteristics will be considered, even if they are not identified as a specific 'market segment'.

### Tailored guidance

Stakeholders raised the need for more detailed guidance on unmetered networks, along with a general request for more illustrative guidance around segmentation. We will continue to evaluate as regulation commences, and we obtain greater information about the market. If it is appropriate, we will consider the development of guidance to support market segments.

Q17. Do you agree, partially agree, or disagree with the proposal that the fair pricing framework would cover all non-domestic consumers, including larger non-domestic consumers?
Q18. If you disagree with the proposal to include all non-domestic consumers within the scope of the fair pricing protections, please specify what changes you would like to see and provide a justification.

Table 9: Response summary for consultation question 17

Response	Number	Percentage
Agree	9	24%
Partially agree	8	21%
Disagree	9	24%
No response	12	32%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

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1.66 In response to consultation questions 17 and 18, 67% of respondents presented an opinion on the inclusion of all non-domestic consumers within the fair pricing framework. Of the total respondents, there was an equal split between those that outright agreed with the proposal and those that did not. A portion of respondents were in partial agreement with the inclusion of non-domestic consumers but gave caveats to their support.

1.67 Many respondents favoured the inclusion of micro and small businesses within the fair pricing framework. Stakeholders highlighted that smaller entities often lack the resources and negotiating power to secure fair terms and effectively behave similarly to domestic consumers, making them more susceptible to poor practices and high costs. One respondent also stated that the monopolistic nature of a heat network means that issues faced by micro and smaller non-domestic consumers will be harder to resolve than in the gas and electricity market. As such, they considered it is important that consumer protection for non-domestic consumers is also strengthened.

1.68 A significant proportion of stakeholders, who disagreed with the proposal, advocated for the exclusion of larger non-domestic consumers. This was a view shared by many respondents who partially agreed with the proposal as well, with the notion that the framework should include micro and small non-domestics but exclude larger consumers. The rationale amongst respondents centred around larger non-domestic consumers being more sophisticated consumers with negotiating power and resources to secure fair agreements with their heat supplier. A minority of respondents also stated that they did not see the reason for distinction between industrial consumers and large non-domestics, given that both categories of consumers will have significant financial and legal capacity to ensure protections are built into their contracts with a heat supplier. Respondents also stated that the inclusion of larger non-domestic consumers risks diluting the framework's focus on those who genuinely need regulatory support and that a more targeted approach would ensure efforts are concentrated where they can deliver the greatest consumer benefit.

1.69 One respondent expanded on their objection to the current proposal by outlining a two-tier non-domestic framework in which small business consumers and large business consumers were separated. Small non-domestics would be fully covered by the fair pricing framework and larger non-domestics would only be subject to transparency requirements. They argued that this approach would balance protection and practicality.

1.70 A few respondents suggested that Ofgem take an iterative approach to incorporating large non-domestic consumers into the framework and review the decision once need and negotiating capacity have been fully assessed. They highlighted that some networks serving a mixture of consumers might differentiate pricing structures to enable more affordable pricing for domestic

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consumers, and where this cross-subsidisation occurs, the framework should not inadvertently discourage the practice.

### **Ofgem response**

#### **Small non-domestics**

We welcome the support from respondents on the need to include micro and small non-domestic consumers within the fair pricing framework. We agree that smaller entities may lack the resources and expertise needed to secure fair contracts and can often behave similarly to domestic consumers. This can result in exposure to poor practices and high costs, making it important that consumer protections encompass non-domestic consumers as well.

#### **Larger non-domestics**

Many respondents questioned the inclusion of larger non-domestic consumers within the framework, and some advocated for their exclusion.

Though we agree that larger non-domestic consumers can possess greater expertise and resources, the heat network supplying these consumers still has market power in that there is a large barrier to moving away from the supplier, especially when compared to the gas and electricity market. We will include larger non-domestic networks within the pricing framework and intend to do further engagement and research with non-domestic consumers to better understand their needs.

#### **Industrial consumers**

Respondents questioned the difference between larger non-domestics and industrial consumers. Industrial networks supply heat for use in industrial processes, for example as pressurised steam, whereas heat networks distribute hot water for space heating. These two types of networks differ significantly in purpose, operation, and in how users utilise them. These differences may require a distinct regulatory approach. At this stage, we do not have sufficient information about this part of the sector to justify extending pricing protections to industrial networks.

#### **Other comments**

There are also practical issues with excluding larger non-domestic consumers, such as the case of subletting. An unintended consequence could also occur in that networks are disincentivised to supply smaller non-domestic consumers if they mostly serve larger non-domestics.

At this stage, we are opting to include all non-domestic consumers, including larger non-domestic, within the pricing framework. Respondents raised concerns about the potential constraint on regulatory resources if larger non-domestics were included. Whilst we acknowledge this point, our aim is to focus regulatory action on the areas of

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the market that are experiencing the greatest level of consumer detriment. We believe that the inclusion of larger non-domestic consumers should not hinder this.

## 2. Cost allocation

### Section summary

Cost allocation refers to how heat suppliers allocate costs to the various charges they levy on consumers, and how prices are structured more generally. Currently, suppliers use diverse pricing structures — including different combinations of connection charges, standing charges, unit rates, and other fixed charges – and allocate different costs to these charges. These differences may complicate price benchmarking. We have previously set out our draft guidance in this area with one prescriptive rule. We considered the creation of prescriptive guidance may limit the ability of heat suppliers to adopt pricing structures that suit their diverse customer bases and business needs, whilst increasing the regulatory burden of reporting, monitoring, and enforcement.

Generally, stakeholder responses agreed with this less prescriptive approach, although many requested clarity and additional examples in key areas.

We have taken this feedback onboard and updated our final guidance in this area as appropriate.

### Question analysis

- Q19. Do you agree, partially agree, or disagree with our approach to cost allocation related to general cost pass-throughs?
- Q20. Do you have suggestions to improve guidance for cost allocation related to general cost pass-throughs?

Table 10: Response summary for consultation question 19

Response	Number	Percentage
Agree	11	29%
Partially agree	16	42%
Disagree	4	10%
No response	7	18%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

- 2.1 11 respondents agreed with the proposed approach to general cost pass-throughs, with 16 respondents partially agreeing and four respondents disagreeing with the proposed approach. Seven respondents did not provide an answer to this question.
- 2.2 A minority of respondents expressed their agreement specifically with the use of activity level as a proxy to apportion costs incurred at a portfolio level across

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networks and application of cost efficiency, which was felt to align with other regulatory frameworks such as those used within electricity distribution. Others welcomed the focus on vulnerable customers as part of the guidance approach.

- 2.3 Despite general agreement with the approach, stakeholders felt there were several areas where the guidance could be strengthened or expanded upon.
- 2.4 Some respondents suggested that the cost allocation guidance in this area should clarify and strengthen its position on efficiency. This included requests to define efficiency/inefficiency, to clarify how efficiency is measured and monitored, and to include examples of acceptable and unacceptable practices in this area. One stakeholder suggested that the guidance should soften its position on the requirement for heat networks to find efficiency savings where possible, amending this point from 'must' to 'expected to'.
- 2.5 Clarity on data reporting and interaction with other regulation was raised with some stakeholders questioning the overlap with HNTAS and the existing obligations in relation to the provision of energy for landlords. Clarity was also requested on a number of general cost allocation points such as greater detail on what data will be collected and required under reporting and what constitutes a controllable vs uncontrollable cost.
- 2.6 Several stakeholders requested examples and guidance for specific sectors such as social housing. Some respondents also felt the guidance should recognise the difference in resource for smaller networks and believed there should be greater flexibility or proportional oversight in these cases.
- 2.7 There was some concern amongst respondents regarding consumer protection and fairness. A minority of respondents emphasised the need to ensure that cost pass through is transparent and fair for consumers. It was also noted that guidance in this area should be careful not to disrupt existing practice in a way which leads to customer detriment (such as penalising customers who may have larger properties but do not necessarily have the income to maintain said properties).
- 2.8 A minority of respondents raised our position on the pass-through of penalties and redress in their feedback. Two felt that specific sectors should be removed from this obligation due to duplication with other legislation (within the leasehold sector) or the structure of ownership meaning residents self-manage a network.

### **Ofgem response**

We welcome feedback from respondents that our approach to general cost pass throughs is broadly considered reasonable. We also welcome feedback from stakeholders on how guidance can be strengthened in this area.

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### Clarity on definitions and examples

We appreciate that the introduction of new regulation may come with some uncertainty and so we have expanded the guidance to provide more specific examples, including references to specific segments where applicable. We have also sought to clarify our positions and provided definitions in many of the areas noted.

### Interactions with other or future regulation

On interactions with HNTAS, we intend to minimise duplications in data reporting across different requirements, and we refer to HNTAS for technical standards and best practices. We may review the data requirements going forward as HNTAS is introduced. We also acknowledge that the guidance may need to consider Landlord and Tenant legislation and has been updated with this in mind.

### Exemptions from prescriptive rule

We disagree, however, that certain market segments should be exempt from the prescriptive guidance regarding pass throughs of penalties and redress. Heat networks are expected to be run efficiently with the aim of providing fair pricing and good consumer outcomes. In cases where compliance and enforcement activities result in redress or penalties, such costs arise from heat networks not achieving the standards that are expected of them and therefore should not be borne by the final consumers. It should be noted, however, that redress or penalties resulting from compliance and enforcement activities will be considered based on all the facts of the individual case, and informed by precedent.

### Other comments

Recommendations specific to benchmarking will be considered when developing our approach.

We have amended our wording in regard to efficiency savings to better reflect the authorisation conditions. As a result use of 'must' in this area has been replaced with 'should'.

Q21. Do you agree, partially agree, or disagree with our approach to cost allocation related to tariff structure?
Q22. Do you have any suggestions to improve guidance for cost allocation related to tariff structure?

Table 11: Response summary for consultation question 21

Response	Number	Percentage
Agree	10	26%
Partially agree	16	42%

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Disagree	4	10%
No response	8	21%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

- 2.9 10 respondents agreed with the proposed approach to the tariff structure, with 16 respondents partially agreeing and four respondents disagreeing with the proposed approach. Eight respondents did not provide an answer to this question.
- 2.10 Several respondents agreed with our cost reflective approach of generally allocating fixed costs to standing charges and variable costs to unit rates. A minority of respondents, however, cautioned that front loading costs onto standing charges could reduce the amount of money available for those in fuel poverty to spend on actual heating. Others noted that it isn't always easy to distinguish between costs which vary with consumption and costs which don't and recommended expanding guidance to cover these cases.
- 2.11 There were also requests for further clarity on this topic including examples, further guidance for specific sectors, examples of acceptable consumption proxies for unmetered networks, and direction on how to make reasonable trade-offs between cost reflectivity and consumer outcomes (particularly for those with a higher proportion of vulnerable customers).
- 2.12 On profit recovery, a minority of respondents asked the guidance to cover alternative approaches to recovery through standing charges and unit rates. Here too, respondents requested examples and for Ofgem to clarify its position in terms of best practice when recovering profit from vulnerable customers. One respondent noted that the draft guidance could lead to directly opposite decisions being taken on similar networks based on different interpretations of the underlying intent of this consideration. Another commented that in certain sectors, such as social housing, flat rate standing charges may be a more predictable option for low-income tenants, and that Ofgem should consider income impacts within the guidance.

### Ofgem response

We welcome feedback that stakeholders broadly agree with our approach to tariff structure cost allocation. As in the previous section, we appreciate stakeholders' desire for clarity and have updated and expanded upon our guidance to provide this where possible.

### Segmentation

We understand that different sectors will require differences in their approach and would encourage authorised persons to consider the principles and potential trade-offs between these areas in decision-making. At this stage, our guidance is unable to

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address every sector specific circumstance and we would again encourage use of the principles to inform and justify decision-making when, if necessary and appropriate, deviating from the guidance best practice approach.

### Impact on fuel poverty

We acknowledge the feedback that following a strict cost reflectivity principle in setting tariff structures can have a significant negative impact on affordability and on fuel poverty. In situations where conflicting principles need to be balanced, deviations from guidance should have a clear rationale and lead to better consumer outcomes.

### Profit recovery

At this stage, due to lack of data and the need for flexibility in the market, we are not including examples of best practice for profit recovery in the guidance, beyond emphasising the need to balance the fair pricing principles and ensuring good outcomes for consumers. We will keep this guidance under review as more data is collected from the market.

Q23. Do you agree, partially agree, or disagree with our approach to cost allocation related to depreciation/capital cost recovery?
Q24. Do you have suggestions to improve guidance for cost allocation related to depreciation/capital cost recovery?

Table 12: Response summary for consultation question 23

Response	Number	Percentage
Agree	10	26%
Partially agree	14	37%
Disagree	4	10%
No response	10	26%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

2.13 10 respondents agreed with the proposed approach to depreciation/capital cost recovery, with 14 respondents partially agreeing and four respondents disagreeing with the proposed approach. 10 respondents did not provide an answer to this question.

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2.14 Several stakeholders raised the possible need for segmentation, particularly noting issues around smaller heat networks in terms of their capital recovery periods and asset management strategies that may differ from those of larger heat networks, and data and resources availability. There were also concerns raised around data availability for legacy networks, and recommendations given on simplified methodologies or proxy depreciation when sufficient data is not available.

2.15 A minority of stakeholders raised the issue that depreciation or capital costs are not recovered through heat network charges, but rather through rent or service charge, highlighting the interaction with the housing legislation.

2.16 On implementation, one respondent commented that there is too much low-level detail, suggesting that there should be one key metric which can evidence that the most appropriate depreciation method based on individual heat networks' circumstances.

2.17 One respondent suggested that there should be more prescriptive rules requiring the recovery of costs associated with depreciation to be spread across the period in question, so operators are building up sinking funds rather than issuing 'shock bills'.

2.18 A minority of respondents raised the risk of the guidance potentially having unintended effects such as increasing the cost of capital or impacting attractiveness of rental properties in the market. One stakeholder argued that increased reliance on recovery through variable charges can reduce revenue stability and certainty and result in increased cost of capital and consumer costs. Another stakeholder echoed similar sentiments, arguing that in certain circumstances it could be better for investors to recover certain capex / depreciation costs through the fixed charge even though the asset is linked to delivering volume (a large heat pump for example) to lower customer prices through a lower cost of capital. It was also mentioned that recovery of the repair and maintenance costs via a standing charge or tariff transfers the responsibility for meeting those costs from the owner to the occupier. This makes the cost of heat in a development with a heat network significantly higher than the cost in a development with a more conventional heating system, which may make properties unattractive on the rental market.

2.19 A few respondents noted that the existing guidance might result in operators deviating from previously agreed arrangements with consumers. Stakeholders cited examples of cases where under existing leases homeowners are required to contribute to the cost of repair and replacement in accordance with their service charge percentage as set out in their lease, leading to larger properties contributing a larger percentage. They considered that replacing this with the draft guidance would mean deviating from previously agreed arrangements.

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2.20 Stakeholders in general also asked for more clarity on the approach, some examples and more information on how to demonstrate compliance with the guidance. One stakeholder asked for further clarification on how operators can demonstrate that their depreciation approach is fair and proportionate without requiring overly complex financial modelling, with another suggesting the provision of model templates for capital replacement reserve calculation. Another respondent asked for more information on minimum depreciation and capital recovery parameters to prevent front-loaded or excessively prolonged recovery periods, and clearer guidance on how replacement and lifecycle investment costs are incorporated and if/how can be recovered prospectively through sinking funds/reserve funds. One respondent asked for more clarity around whether replacement expenditure will be managed similarly to depreciation of assets. Stakeholders also asked for examples around how depreciation can align with lifecycle planning for older or inherited assets, where replacement costs may be uncertain. Finally, one stakeholder asked for clarity in situations where there is a shortfall between the repair cost and what has been collected for repairs, and whether these can be recovered through increase in standing charges/service charges.

2.21 A few stakeholders also provided recommendations on further developing the underlying principle of the approach, for example by aligning the treatment of capital recovery with the ‘fair and reasonable returns’, ensuring adherence to affordability and transparency.

2.22 A minority of respondents questioned the role for Ofgem in providing guidance for capital cost/depreciation recovery, with one stakeholder commenting that they believe Ofgem may be unable to provide helpful guidance on this point before the underlying issue of how heat networks should be dealt with as a service charge item is resolved.

2.23 Finally, it was noted that some heat network providers that operate unmetered networks still utilise standing charges and unit rates based on a proxy for consumption, and this should be reflected in the guidance. We have taken this into account and updated the guidance accordingly.

### **Ofgem response**

We welcome feedback from respondents that our approach to depreciation/capital cost recovery is broadly considered reasonable. We also welcome feedback from stakeholders on how guidance can be strengthened in this area.

### **Interaction with housing legislation**

We acknowledge the interaction between existing housing legislation (the Landlord and Tenant Act) and the implementation of various parts of the pricing framework. As highlighted in the 2025 [ICP Government response](#), we are engaging with MHCLG and DESNZ to further explore this interaction.

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### Segmentation

We acknowledge that flexibility is important given the nascent state of the market and the phase of regulation. The guidance on depreciation is aimed at explaining the underlying principles that should be considered when determining the optimal depreciation method. Given the diversity of the market, we acknowledge that different heat network entities with different characteristics operating in different environments will have different optimal depreciation methods, and the current iteration of the guidance provides the flexibility required for heat networks to optimise their depreciation methods, guided by and balancing the fair pricing principles and objectives.

### Data requirement

Heat network entities are expected to report the categories of costs they recover from different types of charges and how they recover these costs. Please refer to our [regular data reporting draft guidance consultation](#) detailing regular data reporting requirements. In addition, heat networks are expected to retain information such that they will be able to explain their cost allocation practice when required.

### Prescriptive rules

We appreciate the feedback on the need for prescriptive rules on depreciation in order to build up sinking funds to avoid shock bills. At this stage, we are not imposing prescriptive rules on how entities should optimise their depreciation approach due to lack of data, and to avoid sudden and significant increases to consumer bills due to sudden change in depreciation methods. However, we would like to reiterate and emphasise the need to pass on depreciation costs in a timely manner precisely to avoid any shock bills in the future, in line with the fair pricing principles and objectives.

### Recovery through variable charges

We acknowledge the feedback given on recovering some of the depreciation costs that vary with consumption from variable charges. On the point regarding funding uncertainty, if the depreciation of the asset is directly causal to production of heat, this directly links the recovery of said depreciation with the unit rates consumed and paid for. However, we do acknowledge that there may be difficulties for entities to be able to collect the required data point and to accurately estimate the depreciation base required when the value of the depreciation varies with consumption. Deviation from this approach will be assessed contextually in consideration with balancing of additional principles such as cost efficiency, corporate risk, affordability, and others.

### Legacy arrangements

We acknowledge the existing legacy arrangements, which are defined further in guidance as legal and contractual agreements that existed and are legally enforceable before the date 27 January 2026. Deviations from the recommended approaches due to legacy arrangements may be justified, for example due to contractual limitations or that

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they lead to better consumer outcomes. Please refer to our response under the section 'Legacy arrangements' below.

- Q25. Do you agree, partially agree, or disagree with our approach to cost allocation related to bad debt?
- Q26. Do you have suggestions to improve guidance for cost allocation related to bad debt?

Table 13: Response summary for consultation question 25

Response	Number	Percentage
Agree	7	18%
Partially agree	16	42%
Disagree	5	13%
No response	10	26%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

- 2.24 Seven respondents agreed with the proposed approach to bad debt, with 16 respondents partially agreeing and five respondents disagreeing with the proposed approach. 10 respondents did not provide an answer to this question.
- 2.25 One major recurring theme of concern was around the treatment for bad debt for not-for-profit sector, segmentation in general, the need for distinguishing treatments between commercial and social housing contexts, and the interaction with rent/service charges and tenancy law. A few stakeholders also suggested differing treatments between domestic and non-domestic consumers.
- 2.26 A minority of respondents also raised the issue around implementation, focusing on the need to develop mechanism to monitor and benchmark specific input costs including those that relate to bad debt.
- 2.27 There were also concerns about the general approach taken in terms of the ability for entities to recover bad debt. One stakeholder responded that they are concerned about what they interpreted to be the proposal that heat networks should absorb costs where customers struggle to maintain agreed repayment plans, arguing that the guidance appears to create a charter for non-payment, where customers can repeatedly renegotiate payment terms with no consequences. In a similar line of argument, two respondents noted that it is important that the guidance clearly distinguishes between unavoidable debt from genuine consumer hardship and debt arising from ineffective billing or engagement processes, arguing that for small network operators or those with

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legacy sites, the financial impact of non-payment can be far greater due to smaller customer bases and limited cash flow buffers, so preventing debt from occurring in the first place is critical.

- 2.28 Another theme of concerns revolved around the impact of collecting bad debt from consumers. One respondent suggested to ensure that bad debt recovery does not disproportionately impact residents who consistently pay their charges. This was echoed by another respondent that pointed out that consideration needs to be given to how bad debt costs are recovered across the broader customer base and recovering bad debt costs through customer bills on a small communal scheme would have different impacts on the broader customer base than it would on a larger district heating scheme. One stakeholder pointed out the need to recognise regulatory and ethical limits on debt recovery, emphasise the importance of proactive customer engagement and early intervention as part of effective bad debt management. Finally, one stakeholder raised the issue of unintended consequences of the guidance disproportionately affecting smaller networks leading to higher charges for occupiers and rendering the flats in buildings with smaller networks less attractive in rental and sales market.
- 2.29 There were also responses around how the guidance interacts with the principles outlined. A minority of respondents suggested that there should be greater emphasis or weight placed on the principle of affordability and cost efficiency in relation to bad debt and recommended that the guidance be aligned with affordability protections.
- 2.30 In terms of recommendations on how to improve the guidance, one stakeholder recommended amending the guidance around maximising consumer outcomes into consider maximising the consumer outcomes. Stakeholders also asked for more details, clarifications and examples of good practice, specifically around what are the acceptable recovery methods, treatments of historic debt from prior landlords or managing agents, increasing transparency and providing examples for compliant approaches. One stakeholder noted that the details set out are difficult to engage with and is difficult to understand and require further clarification. Another asked for clarity around the use of 'efficient and effective' debt recovery practices, whether these are geared towards the supplier or the consumers.
- 2.31 One stakeholder asked for more clarity on how Ofgem expects the affordability principle to be applied to this context, with another asking for examples of how bad debt might be within the control of a heat network and when the cost arising from such a debt should not be passed on to customers. One stakeholder asked for more details around how to recover the bad debts (standing charge vs unit rate) and the need to balance this against affordability considerations.
- 2.32 Other comments that are out of scope for the current consultation included recommendation to improve future cost allocation rules by possibly including

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component caps to incentivise improved practice, examples on how best to communicate information about bad debt/provision to consumers and the required level of transparency, development of debt socialisation mechanism to deal with unrecoverable debt, and the need for creating a plan and timeline to develop fair mechanism to share consumer debt burden. Some stakeholders also suggested that there is a need for more signposting for those in debt to the energy advice services to ensure right support is available. Few stakeholders also suggested further work on developing longer term solutions for debt-related issues in the heat networks market.

### **Ofgem response**

We welcome the agreement of the majority of respondents with our proposed bad debt guidance approach from stakeholders, but note concerns in this area. We have sought to clarify, where possible, our approach to reassure stakeholders in regard to misconceptions around expected absorption of costs from bad debt by the heat network.

### **Segmentation**

Whilst we recognise that different sectors may have different approaches to bad debt, we believe our guidance in this area is sufficiently high level to accommodate these differences. We understand that different sectors will require differences in their approach and would encourage authorised persons to consider the principles and potential trade-offs between these areas in decision-making. We have attempted to provide flexibility in this area of guidance whilst maintaining a clear focus on consumer protection. At this stage, our guidance is not able to address every sector-specific circumstance and we would again encourage use of the principles to inform and justify decision-making when, if appropriate, deviating from the guidance best practice approach.

### **Debt collection**

We have sought to provide clarity in the guidance in response to concerns raised regarding expectations around heat network debt recovery. We do not expect authorised persons to absorb bad debt costs nor are we encouraging non-payment among customers. We agree with respondents who outlined the importance of effective billing or engagement processes to mitigate the build-up of bad debt and have emphasised this point within our guidance. We recognise concerns about the impact of bad debt on smaller networks and the difference between heat networks and the wider gas and electricity market in this regard due to the limited number of customers within a network across which to spread unrecoverable bad debt costs. Whilst debt socialisation is outside the scope of this guidance this area is being explored further by DESNZ.

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### Alignment with principles

Our guidance in this area is built around the pricing principles, with affordability forming a key component of the guidance for bad debt cost allocation. We also recognise that there will be ties within this guidance to broader regulation in this space (such as consumer protection guidance) and have sought to make these connections clear where possible.

### Examples and clarity

We have updated the guidance to include examples in key areas and to offer clarity where possible. However, we are not at this stage able to offer an example for every circumstance and advise use of the principles in decision making.

Q27. Do you agree, partially agree, or disagree with our approach to cost allocation related to corporate risk?

Q28. Do you have suggestions to improve guidance for cost allocation related to corporate risk?

Table 14: Response summary for consultation question 27

Response	Number	Percentage
Agree	10	26%
Partially agree	13	34%
Disagree	4	10%
No response	11	29%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

2.33 10 respondents agreed with the proposed approach to corporate risk, with 13 respondents partially agreeing and four respondents disagreeing with the proposed approach. 11 respondents did not provide an answer to this question.

2.34 The main theme of concern raised by stakeholders is around the relationship between the guidance on corporate risk and the uncertainty of future connections and investment risk. Some stakeholders highlighted the issue around accurately forecasting future customer numbers and uncertainty around capital cost allocation, with one stakeholder raising caution that projects where the upfront capital costs can only be recovered once a certain number of additional consumers have connected will be perceived as far riskier, and therefore less likely to be supported, than those where costs can be recovered based on the core, committed consumer base at the outset of the network. In a similar line of argument, another stakeholder mentioned that currently, most district heat networks do not have any certainty regarding the number of customers or the speed or extent to which a network will grow and achieve connections. One

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stakeholder suggested re-wording the guidance of this section to recognise their view that heat networks are not a monopoly within the context of wider heating market. They further argued that it is impossible to spread the recovery of costs over a large number of unknown customers, and that heat networks may be required to spread the recovery of costs over smaller group of customers induce investment, which they do not see as an issue because consumers are not compelled to join the heat network.

- 2.35 The need for segmentation is another key theme that was frequently mentioned, with one stakeholder mentioning that for small network operators or operators with legacy sites, corporate risk can be more concentrated and less diversified, meaning that proportionate flexibility is essential. Another stakeholder highlighted the cases around not for profit where the risk is borne at portfolio level and not priced into the charges, arguing that network-specific risk premiums are not appropriate for not-for-profit providers.
- 2.36 A minority of stakeholders argue that the current drafting of the guidance provides too much flexibility, allowing operators to justify inflated returns by invoking 'corporate risk' without clear evidentiary standards, and recommended that Ofgem should issue defined parameters for risk and link them to measurable indicators such as debt ratio, network size, or contractual exposure, and require transparent disclosure of risk allocation across shareholders, funders, and consumers, ensuring that risks retained by investors are not unfairly transferred into tariffs. They also emphasised that corporate risk allowances should not compensate for inefficiency, poor asset design, or speculative investment.
- 2.37 Stakeholders also asked for more clarity, including around how the upfront and initial costs can be factored into tariff models especially as many heat networks are part of phased long-term developments, definition on 'improper' recovery of initial capital costs & capital expenditures and what constitutes corporate risk for both commercial and not-for-profit heat network operators, and provide examples relevant to social housing, specifically around equitable capital cost recovery when networks expand. Suggestions to improve guidance also included more information on how we will assess whether a risk allowance or return level is considered reasonable, including further guidance on acceptable approaches to demonstrating prudent financial management and risk mitigation such as maintaining appropriate reserves, insurance coverage, and transparent reporting, confirming that not-for-profit operators may allocate overheads using simplified portfolio ratios, and providing guidance on treating insurance and contingency costs separately. One stakeholder also recommended replacement of the word 'improper' with another word / phrase which doesn't carry the connotation of wrongdoing.
- 2.38 Some concerns around implementation were also raised, specifically around ensuring proportionality in oversight, and supporting transparency and accountability.

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2.39 Other comments included one stakeholder mentioning the possible unintended consequences of impact on the rental market in buildings which have heat networks which in turn may depreciate the value of the leasehold interest, and another commenting that they do not believe it is useful for Ofgem to regulate this area at this stage.

### **Ofgem response**

#### **Impact of guidance on investment risk and growth**

We acknowledge the limitations around accurate forecasting of future customer numbers. At this stage, our guidance does not provide prescriptive rules around corporate risk but rather outlines some of the principles-based approaches that may be appropriate when making decisions involving corporate risk. Regarding the uncertainty around future consumer numbers, our guidance encourages entities to use the principles outlined in the fair pricing guidance along with the best information available at the time, acknowledging the uncertainty around such estimations.

#### **Segmentation and flexibility**

At this stage of the regulation, we acknowledge the need for flexibility to account for varying practices across different segments of the market. Deviations from our guidance may be appropriate if they can be justified on the basis of fair pricing principles, and consumer and industry outcomes.

#### **Implementation**

As mentioned in our previous consultations and government consultation responses, we aim to be proportionate in our regulatory oversight, acknowledging the diversity of the market and the level of maturity of the market, along with increasing transparency and accountability through the fair pricing framework.

Q29. Do you agree, partially agree, or disagree with our approach to cost allocation related to fuel procurement?
Q30. Do you have suggestions to improve guidance for cost allocation related to fuel procurement?

Table 15: Response summary for consultation question 29

<b>Response</b>	<b>Number</b>	<b>Percentage</b>
Agree	14	37%
Partially agree	10	26%
Disagree	3	8%
No response	11	29%

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*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

2.40 14 respondents agreed with the proposed approach to fuel procurement, with 10 respondents partially agreeing and three respondents disagreeing with the proposed approach. 11 respondents did not provide an answer to this question.

2.41 Flexibility is a key theme raised by the stakeholders, arguing that flexibility in procurement is important particularly for small network operators or operators with legacy sites due to differences in buying power or access to long term fixed price contracts, and that the guidance should recognise the diversity of fuel procurement approaches across the heat network industry, for example waste heat or purchasing fuel on a portfolio basis and the range of practices in the market.

2.42 A minority of stakeholders highlighted the interaction between the guidance and other legislation and/or regulations, including the need for social landlords to have competitive procurement rules, duplication or conflict with existing law such as the Landlord and Tenant Act.

2.43 Some of the improvements to the guidance proposed include clearer examples of best practices, and clarity on the evidence or documentation required. Stakeholders demanded more clarity on what would constitute an acceptable procurement practice for smaller networks, what are the minimum standards for documenting procurement decisions (particularly around Third-Party Intermediaries otherwise known as TPIs), how to evidence the procurement strategy, and what would be deemed as compliant based on the same principles of a 'fair and reasonable' test. Respondents also asked for clarification on the treatment of bulk-purchased energy serving multiple networks through portfolio contracts.

2.44 Other comments that are out of scope for the current guidance include recommendations for sharing market insights to support efficient collective purchasing, the need for effective market mechanism for fuel procurement, and placing requirements on gas and electricity suppliers to be in a position to identify its heat network customers.

### Ofgem response

We welcome feedback from respondents that our approach to fuel procurement recovery is broadly considered reasonable. We also welcome feedback from stakeholders on how guidance can be strengthened in this area. In line with some of the feedback received, we have decided to move the fuel procurement section in cost allocation to the fair pricing principles guidance.

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### Flexibility

We acknowledge the feedback from stakeholders that outlined the need for flexibility in fuel procurement strategies, particularly around small heat networks or legacy heat networks. We agree that factors out of the control of the entities such as differences in buying power or access to longer term contracts can drive legitimate differences in fuel procurement strategies. The aim of the guidance is to provide an illustration of the underlying approach that should be taken when devising procurement strategy, which is to use the various principles outlined to ensure that the procurement strategy is beneficial to the final consumers. At this stage, the guidance does not provide prescriptive rules around fuel procurement strategies due to lack of data regarding current practices and the need for flexibility as the market adjusts to regulation. The current iteration of guidance should provide the flexibility needed for different entities to be able to make the optimal procurement decisions, whilst simultaneously ensuring that those decisions are driven by fair pricing principles with optimal consumer outcome in mind.

### Interaction with other legislations

We acknowledge the interaction between existing housing legislation (the Landlord and Tenant Act) and the implementation of various parts of the pricing framework. As highlighted in the [2024 ICP consultation](#), we are engaging with MHCLG and DESNZ to further explore this interaction.

### Other comments

Comments from stakeholders around the need for sharing of market insights and effective mechanism for fuel procurement, along with the suggestions of placing requirements around gas and electricity suppliers to identify their heat network customers have been noted but remains out of scope for the current iteration of guidance.

Q31. Do you agree, partially agree, or disagree with our approach to cost allocation related to fair and reasonable returns?
Q32. Do you have suggestions to improve guidance for cost allocation related to fair and reasonable returns?

Table 16: Response summary for consultation question 31

Response	Number	Percentage
Agree	6	16%
Partially agree	15	39%
Disagree	5	13%
No response	12	32%

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*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

- 2.45 Six respondents agreed with the proposed approach to fair and reasonable returns, with 15 respondents partially agreeing and five respondents disagreeing with the proposed approach. 12 respondents did not provide an answer to this question.
- 2.46 Several stakeholders had concern about the overall approach to fair and reasonable returns, and the possible impact on the market. One stakeholder raised the concern that capping rate of return that is tied to risks associated with the investment may have the unintended consequences of reduced incentives to make savings on procurement and other costs or driving smaller suppliers/operators out of the market. Another stakeholder fundamentally disagreed with the approach of profitability monitoring and for Ofgem to investigate in cases where it identifies concerns, arguing that the lack of clarity around the expectations of what constitutes a fair and reasonable return will create uncertainty for heat networks and their investors and will have adverse effects on the heat network market and stifle future growth, which is echoed by another stakeholder who stated that the current guidance risks adding uncertainty and lowering investment confidence. Finally, a minority of stakeholders also asked for confirmation that the fair and reasonable returns will not apply to heat networks which operate on a strict cost recovery only model.
- 2.47 Stakeholders brought up the need to interpret fair and reasonable returns within the context of scale, access to finance and the relative cost of capital, particularly for smaller entities. They cautioned that imposing a uniform benchmark across the sector could unintentionally penalise smaller operators and discourage investment in older or more complex networks that require ongoing capital support.
- 2.48 Conversely, some stakeholders raised issues and risks regarding the profits that are earned by heat networks. One stakeholder brought up the importance of protecting affordability and ensuring that return allowances do not lead to disproportionate price increases for vulnerable residents. Another stakeholder proposed that the guidance should adopt a more preventative approach, with mechanisms such as price caps. One respondent rejected the notion that a monopoly should have the option to make any returns as consumers did not choose the suppliers and therefore the suppliers should not make profit at the expense of the consumers.
- 2.49 A minority of stakeholders recommended some changes in wording along with additional information that should go into guidance. One stakeholder suggested replacing 'higher than expected' with 'outside of [X] standard deviations of the mean' for the given network archetype based on Ofgem data gathering and analysis. Another stakeholder suggested that section 2.88 be amended to remove

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references to profits at a ‘competitive level’, as it is unclear that ‘competitive profit’ is a useful concept in the context of monopolistic heat networks, and that the phrasing ‘level of profit to provide a fair return on investment’ in 2.87 is much clearer and more appropriate.

- 2.50 Topics that were raised by stakeholders that they propose be added to the guidance included defining what is fair and reasonable, listing out factors that would be considered as appropriate levels of returns, including a notional upper limit for returns in order to provide certainty to customers and help set expectations, providing greater clarity on how Ofgem will determine whether returns are fair and proportionate, including what evidence operators may be expected to provide, using illustrative examples or indicate reference points rather than fixed thresholds to ensure flexibility whilst maintaining consistency, and providing examples of best practice for social housing.
- 2.51 Stakeholders also asked for clarity on how to account for returns within cost allocation practices to avoid double charging, whether consideration will be given to the context that many authorised persons will be managing multiple networks at varying stages of development, and the treatment of legacy assets and how older infrastructure and past investments should be reflected in pricing to avoid unfair cost burdens on current residents.
- 2.52 Other comments that are outside the scope of this guidance include the need to recognise cross subsidy within housing portfolios as legitimate as spreading profitability across the portfolio avoids the need to raise tariffs on underperforming networks, consideration of portfolio level profitability, the scale of deviation from averages that will be used for profitability benchmarking, publication of returns statistics in a transparent and easy to understand way (without naming networks) to allow investors to understand where their networks might be at risk of an investigation, and the need for a definition of ‘not-for-profit,’ as this underpins many compliance pathways. Finally, one stakeholder argued that segmentation is important, and that metrics must be differentiated between profit and not-for-profit entities, proposing that the guidance allows not-for-profit providers to evidence reasonableness through governance and reinvestment records rather than financial ratios.

### **Ofgem response**

#### **Overall approach to fair and reasonable returns**

Our framework for fair pricing consists of both consumer and industry outcomes embedded within the framework. We acknowledge the concerns around the lack of clear levels of acceptable profits and the uncertainty around it. At this stage we are unable to provide a range of ‘acceptable’ level of profits due to the diversity of the market, the phase of regulation and the lack of data. We are also not providing the ‘acceptable’ levels of returns at this stage to give the market the flexibility and

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encourage growth, whilst ensuring good pricing outcomes for consumers, including affordability. We would encourage heat networks to consider the fair and reasonable returns principle when deciding the prices such that the benefits from efficient running of the heat networks can translate to both good consumer outcomes and profitable investments that can drive industry growth. Any analysis on fair and reasonable returns will take into account the context of the heat network and balance industry outcomes with consumer outcomes.

### Other comments

Comments from stakeholders around cross subsidy are addressed in the relevant fair pricing principles section. Feedback on data segmentation, assessment of profitability and publication of data outside the scope of this guidance but will be taken into consideration under relevant areas accordingly.

We will not provide a definition of not-for-profit networks within the guidance. As a non-specific term, we do not consider it to be helpful when discussing particular market segments. We do, however, refer in our guidance more specifically to purely cost recovery heat networks, which includes many not-for-profit models.

Q33. Do you have suggestions to improve guidance for cost allocation related to penalties and redress?

Table 17: Response summary for consultation question 33

Response	Number	Percentage
Yes	20	53%
No	18	47%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

- 2.53 We received a total of 16 comments to this question about pass through of penalties and redress.
- 2.54 A minority of responses asked for more clarity on how the policy would deal with third party relationships, specifically around the issue of passing of fines and penalties when the issue is not the fault of the operator (e.g. gas network failures, a third party provider making the mistake), and Ofgem's view on pricing of risk of penalties and redress via third party contracts.
- 2.55 Several respondents also brought up implementation issues, mainly around how the compliance to this policy is expected to be reported and monitored, how this would interact with the housing legislation of Landlord and Tenant Act, and the need for proportionate reporting for smaller networks and the need for transition period, especially for older heat networks.

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2.56 Some respondents noted the issues around how this would work for not-for-profit heat networks and asked for more clarity, particularly around how not-for-profit networks should account for these payments if they cannot be passed on, noting the risks of increasing other charges and passing them on to final consumers, or reducing service quality.

2.57 Finally, a minority of respondents suggested that the guidance should include suggestions of reinvesting savings from avoided penalty to improving infrastructure, and supporting customers in vulnerable circumstances.

### **Ofgem response**

We welcome feedback from stakeholders on this question. As we consulted on this policy previously, we have only asked for feedback on how to improve the guidance vis-à-vis the policy in this consultation.

### **Third party relationships**

Authorised entities are ultimately responsible for the provision of services to consumers and as such, any issues that can result in penalties and redress that are determined to be within the control of the authorised entity (this includes when an authorised person outsources or subcontracts services to a third party) will be levied onto the authorised entity. Any enforcement actions that may result in penalties or redress will consider all the relevant facts of the case, which may include the causal and contributing factors of the breach of regulation and the level of control that the authorised entity have over the factors.

While our position on Guaranteed Standards Of Performance (commonly referred to as GSOPs) for heat networks is subject to further consultation, we may explore an approach similar to gas and electricity, where the supplier is responsible for meeting GSOP obligations and for ensuring any compensation is passed through to the end consumer. We would, however, expect organisations to agree clear contractual terms with relevant third parties regarding GSOP responsibilities and cost recovery prior to entering into such arrangements.

### **Data reporting and compliance**

The [regular data reporting draft guidance consultation](#) outlines the data that needs to be submitted to the regulator on an enduring basis. Amongst those data points, the cost stack of the tariff must be reported regularly. The proposed benchmarking approach of own prices over time combined with the reporting of cost stack can help indicate instances where such redress and penalties may have been passed onto final consumers,

### **Interaction with Landlord and Tenant Act**

We have been working with industry and across government to understand the interaction with existing housing legislation. As part of the [2025 ICP government response](#), DESNZ set out that they are working with the Ministry for Housing,

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Community, and Local Government (MHCLG), as well as the Welsh and Scottish Governments, to further explore options for unbundling heat charges from housing charges. As part of this work, they will be exploring a number of legislative and practical impacts, including the relationship between existing leases and housing law.

### Proportionality and not-for-profit entities

Heat networks are expected to be run efficiently with the aim of providing fair pricing and good consumer outcomes. In cases where compliance and enforcement activities result in redress and penalties, such costs arise from the heat networks not achieving the standards that are expected of them and therefore should not be borne by the final consumers. As in the [2025 ICP government response](#), following an analysis of consultation responses, and subsequent stakeholder engagement, we are consulting further on our proposals. on GSOPs, with 2027 being the earliest date to phase in GSOP policies. In developing these proposals, we will take note of stakeholder suggestions, which included a tiered approach to compensation payments, and the further phasing-in of GSOPs to give authorised persons more time to adjust their network infrastructure.

### Reinvestment of avoided penalties

We acknowledge the need for investment in infrastructure to improve consumer outcomes, and the importance of supporting customers in vulnerable circumstances. We also encourage avoidance of penalties by suppliers and operators working collaboratively and constructively to comply with the principles. We cannot currently speculate on the notion of re-investment of avoided penalties as there is no methodology to quantify this approach with a newly regulated market.

Q34. Do you agree, partially agree, or disagree with our approach to cost allocation related to legacy arrangements?
Q35. Do you have suggestions to improve guidance for cost allocation related to legacy arrangements?

Table 18: Response summary for consultation question 34

Response	Number	Percentage
Agree	13	34%
Partially agree	8	21%
Disagree	2	5%
No response	15	39%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

2.58 13 respondents agreed with the proposed approach to legacy arrangements, with eight respondents partially agreeing and two respondents disagreeing with

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the proposed approach. 15 respondents did not provide an answer to this question.

- 2.59 Respondents who agreed with the guidance noted that the approach is proportionate given the existing legal obligations in the market, and recognised the challenges for operators that inherit pre-existing contractual or technical setups, especially for small networks operators or operators managing legacy sites. One respondent cautioned that affordability should be protected and to ensure legacy cost recovery does not lead to disproportionate pricing for vulnerable residents.
- 2.60 Several respondents noted the need for more clarity around deviations from the guidance due to legacy arrangements. A minority of respondents suggested that Ofgem should require entities to document reasons for deviation from the cost allocation guidance, and document the steps that will be taken to move towards compliance. In situations when outcomes can be improved by deviating from the guidance, this should be accompanied with clear set of evidence. Another stakeholder noted that the deviation due to legacy arrangement should not be prolonged longer than required, with another stakeholder recommending that there should be timescale for resolution of the legacy arrangement.
- 2.61 Stakeholders also asked for clearer criteria or examples of acceptable deviations due to legacy arrangements, what legacy costs are reasonable to recover and which ones should be excluded/phased out to avoid unfair burdens on consumers, what set of evidence should be required to justify them. They also asked for clarity from Ofgem on how the legacy costs will be phased out or reallocated over time, and for Ofgem to provide clear timeline to transition to full compliance.
- 2.62 The responses also indicated the need for clearer definition of legacy, with one stakeholder recommending using build completion date or original ownership structure. Another stakeholder asked for clarity on how Ofgem plans to assess the transitional arrangements.
- 2.63 One stakeholder noted that the guidance should recognise the costs of bringing legacy sites (interpreted as existing heat networks prior to regulation) up to current standards and that such costs should be recoverable in fair and transparent ways provided they result in improved consumer outcomes.
- 2.64 Finally, one stakeholder recommended simplified data submissions for older schemes that lack digital records.

### Ofgem response

We welcome feedback that a majority of stakeholders that responded broadly agree with our approach to legacy arrangements. As in the previous section, we appreciate stakeholders' desire for clarity and have updated and expanded upon our guidance to provide this where possible.

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### Deviations from guidance

We acknowledge stakeholders' feedback on the need for clarity on how to document deviations from guidance and how Ofgem would evaluate such deviations. This will form part of our upcoming policy development and consultation on how Ofgem will investigate and determine disproportionate pricing and as such is out of scope for this guidance.

### Definition of legacy arrangements

As discussed in our cost allocation guidance, legacy arrangements refer to contractual agreements made prior to regulation which cannot be broken or renegotiated by authorised persons.

### Cost of bringing existing heat networks up to standards

When entities incur costs to improve their existing heat networks to become compliant with the regulation and/or to provide improved consumers outcomes, those costs should be passed onto final consumers as part of the provision of heat. However, we would also expect authorised entities to consider the impact on customers when recovering these costs, such as the appropriate method of depreciation and using an adequate time horizon for recovery as discussed within our cost allocation guidance.

### Simplified data submissions

For networks with limited historical data, we would like to clarify that historical pricing data beyond the first reporting period (including backdating) will not be required for Ofgem's regular data reporting (see [regular data reporting draft guidance](#)). For networks with limited historical data, please see our response under Q13, page 29.

Q36. Do you agree, partially agree, or disagree with our approach to cost allocation related to connection charges?

Q37. Do you have suggestions to improve guidance for cost allocation related to connection charges?

Table 19: Response summary for consultation question 36

Response	Number	Percentage
Agree	11	29%
Partially agree	9	24%
Disagree	3	8%
No response	15	39%

*Please note that the above percentages are rounded to the nearest full figure and therefore may not sum up to 100%*

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2.65 11 respondents agreed with the proposed approach to connection charges, with nine respondents partially agreeing and three respondents disagreeing with the proposed approach. 15 respondents did not provide an answer to this question.

2.66 Flexibility is a key theme that was raised among stakeholders. One respondent noted that the approach would restrict flexibility and innovation in tariff structures, suggesting that Ofgem revise the guidance to indicate acceptance for a wider range of accepted tariff methodologies, in line with industry practices. Another respondent echoed the sentiment, arguing that for small network operators and legacy sites, flexibility is essential, as connection costs vary widely depending on layout, existing infrastructure, and the absence of economies of scale. The guidance should explicitly acknowledge that connection charges may legitimately differ between customers due to connection size, technical complexity, or location within the development. Operators should be permitted to apportion costs accordingly so that more complex or higher-capacity connections contribute proportionately more. Flexibility was also noted in terms of non-domestic customers, with one stakeholder noting that it is important to recognise that some non-domestic customers may wish to pay a lower connection charge, with the additional ESCO investment repaid over time via a supplemental fixed charge / financing charge. This flexibility of approach to meet customer needs should not be constrained or prevented by the guidance. A few stakeholders also provided proposals on different models to treat connection charges. Some of the models proposed include uniform pricing across the network based on the cost of connection related to capacity connected, uniform pricing by customer type.

2.67 Stakeholders also raised concerns around transparency, with one stakeholder commenting that connection charges should be clearly communicated and must not undermine affordability, especially for vulnerable residents. One stakeholder recommended that connection charges be standardised as far as possible, with transparent cost components and clear distinction between developer contributions and consumer charges.

2.68 There were also concerns raised about the potential of conflicting sections of guidance or conflicts between the guidance and zoning regulations. One stakeholder noted that requiring that the 'connection charges to new consumers are no less than the incremental cost of connecting to new customers' is not necessarily aligned with the principle which recognises that 'in order to ensure upfront capital costs are recovered efficiently, authorised persons should consider, in the case of district heat networks, accounting for changes in customer numbers over time as more buildings connect to the network'. They argued that these two principles could lead to conflicting interpretations in practice, and further clarity would be helpful on how cost-reflective pricing interacts with phased cost recovery in heat network development. Another stakeholder raised the issue of zoning, mentioning that connection charge caps

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are likely to be a feature of heat network zoning, as may be some wider local price controls or expectations, none of which are referenced in any of Ofgem's publications on heat network regulation to date. They considered that this has the potential to create two directly contradictory regulatory expectations.

Finally, one stakeholder recommended the removal of the stipulation (2.107) that 'Authorised persons should consider ensuring that the connection charges to new consumers are no less than the incremental cost of connecting to new customers' given this is at odds with fair and transparent pricing and may directly contradict connection charge caps brought forward as part of heat network zoning.

2.69 Several stakeholders disagree with the proposed approach to connection costs. One stakeholder argued that connection charges are normally paid by building owners when connections are made, and allocating these costs to standing charges to end users can have adverse effects on affordability. Another argued that the expectation that connection charges are 'no less than the marginal cost' to connect an additional consumer risks greater inconsistency in application (e.g. where an early customer on a new leg of a network effectively pays a much greater connection charge than later adopters on the same leg).

2.70 A minority of stakeholders asked for more clarity on guidance for historical costs, such as when the costs have already been recovered in house prices and more information on how legacy connection charges can be recovered. Others asked for more clarity in the guidance on up front connection charges, and whether the guidance refers to the charges from heat networks that are levied to the building owners, or whether they refer to the recovery of the charges by the building owner from the tenants/leaseholders. One stakeholder mentioned that the guidance should explicitly prohibit retrospective connection cost recovery from consumers where those costs have already been covered through development finance or capital grants. Few stakeholders asked for examples.

### Ofgem response

We welcome feedback that stakeholders broadly agree with our approach to connection charges. As in the previous section, we appreciate stakeholders' desire for clarity and have updated and expanded upon our guidance to provide this where possible.

### Flexibility

We acknowledge the respondents' concerns around the need for flexibility and the possible impact of the guidance on restricting innovative tariff structure. We agree that flexibility at this stage of the regulation is needed to accommodate the diversity of the market, but we disagree that the current guidance would restrict innovative tariff structures. The guidance is not intended to provide a prescriptive rule at this stage but rather provide the underlying approach that is based on the principles outlined in the fair pricing guidance. We acknowledge the diversity of heat networks in the market and

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acknowledge that the diversity in terms of connection size, and technical complexity can lead to legitimate differences in connection charges and different optimal connection charges models. Heat network entities are expected to balance various principles outlined in the fair pricing principles in their connection charges methodologies and tariff structures. We acknowledge that different heat networks operating within different contexts will be balancing such priorities differently, and that the guidance has been drafted with this need for flexibility in mind.

### **Transparency**

We agree that connection charges to consumers need to be transparent, as set out in consumer protection guidance, we would expect all suppliers to provide heat network consumers with accurate and timely bills that are easy to understand. At this stage, we are unable to provide a standardised method to connection charges due to lack of data. However, we will keep this policy under review as regular data are collected from the market.

We acknowledge that there may be some concerns around the fairness of recovering connection charges from a mixture of freehold and leasehold occupants due to the difference in ownership. We encourage authorised persons to consider the consumer impact principle when making decisions on how to recover connection charges from a mixed consumer base such as this.

### **Conflicting principles**

We acknowledge that under certain circumstances, adherence to one principle may result in conflict with another principle. For example, this may happen when adherence to strict cost reflectivity may come at the expense of the affordability principle or minimising corporate risk. Under such circumstances, we expect entities to apply their best judgement in balancing the various principles and objectives that are specified within the fair pricing framework specific to their circumstances. When deciding whether an entity has breached any of the underlying principles of the cost allocation guidance, we will consider both the context and the justification of prioritising other possibly conflicting principles.

### **Conflicting approach with zoning**

We are working closely with DESNZ to ensure that the interaction between zoning conditions and Ofgem pricing regulations are clear.