

# **Subsidy Advice Unit Report on the proposed modified Green Heat Network Fund subsidy scheme**

**Referred by the Department for Energy Security  
and Net Zero**

**10 April 2026**

**Subsidy Advice Unit**

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Part of the Competition and Markets Authority



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# 1. The Referral

- 1.1 On 19 February 2026, the Department for Energy Security and Net Zero (DESNZ) requested a report from the Subsidy Advice Unit (the SAU)<sup>1</sup> in relation to the proposed modified Green Heat Network Fund subsidy scheme (the GHNF Scheme) under section 52 of the Subsidy Control Act 2022 (the Act).<sup>2</sup>
- 1.2 This report evaluates DESNZ's assessment of compliance (the Assessment) of the GHNF Scheme with the requirements of Chapters 1 and 2 of Part 2 of the Act.<sup>3</sup> It is based on the information and evidence included in the Assessment.
- 1.3 This report is provided as non-binding advice to DESNZ. It does not consider whether the GHNF Scheme should be implemented, or directly assess whether it complies with the subsidy control requirements.

## Summary

- 1.4 The Assessment uses the four-step structure described in the Statutory Guidance for the United Kingdom Subsidy Control Regime (the [Statutory Guidance](#)) and as reflected in the SAU's Guidance on the operation of the subsidy control functions of the Subsidy Advice Unit (the [SAU Guidance](#)).
- 1.5 In our view, DESNZ has considered in detail many aspects of the compliance of the GHNF Scheme with the subsidy control and energy and environment principles. In particular, the Assessment:
  - (a) clearly describes and evidences the specific policy objective of the GHNF Scheme and how it relates to wider government objectives regarding heat networks (Principle A);
  - (b) clearly sets out the positive effects of the GHNF Scheme in relation to the policy objective as well as potential negative impacts, and conducts a balancing exercise between them in line with the Statutory Guidance (Principle G); and
  - (c) clearly explains and evidences how the GHNF Scheme complies with Principles A and B of the Energy and Environment Principles.

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<sup>1</sup> The SAU is part of the Competition and Markets Authority.

<sup>2</sup> [Referral of the proposed modified Green Heat Network Fund subsidy scheme by the Department for Energy Security and Net Zero - GOV.UK.](#)

<sup>3</sup> Chapter 1 of Part 2 of the Act requires a public authority to consider the subsidy control principles and energy and environment principles before deciding to give a subsidy. The public authority must not award the subsidy unless it is of the view that it is consistent with those principles. Chapter 2 of Part 2 of the Act prohibits the giving of certain kinds of subsidies and, in relation to certain other categories of subsidy creates a number of requirements with which public authorities must comply.

- 1.6 However, we have identified the following areas for improvement. The Assessment should:
- (a) focus on, and explain why, non-subsidy options - such as commercial loans or equity investments - were not considered appropriate to achieve the policy objective (Principle E);
  - (b) more clearly explain what would happen in a counterfactual scenario where the GHNF Scheme is not implemented (Principle C);
  - (c) as part of the consideration of proportionality (Principle B):
    - (i) provide further detail on the financial tests used to verify that the costs of each project do not exceed the minimum necessary;
    - (ii) explain and evidence in more detail how DESNZ arrived at the caps that limit the size of awards; and
    - (iii) consider how the possibility of cumulation impacts the assessment of the proportionality of individual awards; and
  - (d) consider in more detail the competitive outcomes expected in the market for the supply of heat as a result of the Scheme (Principle F).
- 1.7 We discuss these areas below, along with other issues, for consideration by DESNZ in finalising its assessment.

## The referred scheme

- 1.8 The GHNF Scheme was introduced in 2022 and aims to support the commercialisation and construction of new low-carbon heat networks (including the supply of cooling) and the retrofitting and expansion of existing heat networks. Heat networks distribute thermal energy in the form of steam, hot water or chilled liquids from a central source of production through a network of pipes to multiple properties for the use of heating, cooling or hot water.<sup>4</sup> Heat networks form an important part of the government's plan to reduce carbon and cut heating bills for customers.<sup>5</sup> Funding through the GHNF Scheme is disbursed through a series of funding rounds. The GHNF Scheme is now in its 11th funding round.<sup>6</sup> DESNZ propose to modify the GHNF Scheme, by increasing its budget, from April 2026.

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<sup>4</sup> See [Heat networks - GOV.UK](#).

<sup>5</sup> Heat networks offer carbon emissions savings by supplying heat to buildings from a central source, avoiding the need for households and workplaces to rely on individual, energy-intensive heating solutions such as gas boilers. Low-carbon heat networks utilise technologies such as heat pumps, recovered heat, energy from waste and geothermal.

<sup>6</sup> See [Green Heat Network Fund \(GHNF\): Round 11 application guidance](#).

- 1.9 The GHNF Scheme is open to applicants from organisations in the public, private and third sectors who are responsible for the development of heating networks (including cooling networks) in England and Wales<sup>7</sup> that meet gated application metrics. These metrics<sup>8</sup> include a threshold for carbon intensity of heat delivered by the heat network,<sup>9</sup> consumer detriment,<sup>10</sup> the minimum annual heat energy demand and the applicant project's social internal rate of return (IRR). Applications are assessed by a third-party delivery partner to DESNZ, who make recommendations to a DESNZ investment committee.
- 1.10 Applicants can apply for commercialisation costs, construction costs, or both. Eligible commercialisation costs include costs relating to final contract negotiation, procurement of the heat network delivery, planning requirements, environmental impact assessment and geological surveys. Eligible construction costs include costs relating to all aspects of building a heat network which include accessing sources of low-carbon heat, construction of energy centres and thermal stores, laying of pipes and installation of heat interface units (HIUs) and metering and controls in premises.
- 1.11 Applicants may apply for a maximum allowable grant of up to, but not including, 50% of the estimated eligible commercialisation and construction costs of the project. The GHNF Scheme will award no more than 4.5 pence of grant per 1 kilowatt-hour (kWh) of heat delivered to customers over the first 15 years of operation. There will be an upper limit of £1 million for commercialisation funding. However, if an applicant evidences a compelling strategic requirement for a higher award, DESNZ reserve the right to increase the limit for that project.
- 1.12 DESNZ explained that the GHNF Scheme is a Scheme of Particular Interest because it allows for the provision of one or more Subsidies of Particular Interest to be given.<sup>11</sup> In particular, DESNZ stated that the GHNF has undergone significant change in the form of an increase in budget of more than 25%, meaning it cannot be treated as a permitted modification,<sup>12,13</sup> and individual beneficiaries are able to receive awards greater than £25 million under the GHNF Scheme.

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<sup>7</sup> On 7 April 2026, DESNZ announced that the GHNF had been expanded to fund projects in Wales, having previously been limited to funding projects in England only - [Welsh households to save money on bills through heat networks expansion - GOV.UK](#).

<sup>8</sup> For further information see [Green Heat Network Fund \(GHNF\): Round 11 application guidance](#), page 13.

<sup>9</sup> This metric, referred to as 'carbon gate', requires every funded heat network to stay below a carbon intensity limit of 100 grams of carbon-dioxide-equivalent per kilowatt-hour of heat delivered.

<sup>10</sup> See paragraph 2.40.

<sup>11</sup> Within the meaning of regulation 3 of [The Subsidy Control \(Subsidies and Schemes of Interest or Particular Interest\) Regulations 2022](#) and [The Subsidy Control \(Subsidies and Schemes of Interest or Particular Interest\) \(Amendment\) Regulations](#) which set out the conditions under which a subsidy or scheme is considered to be of particular interest.

<sup>12</sup> DESNZ have told us that the GHNF Scheme budget will be increased by £490 million from April 2026.

<sup>13</sup> See paragraph 9.8 to 9.18 of the Statutory Guidance.

## 2. The SAU's Evaluation

2.1 This section sets out our evaluation of the Assessment, following the four-step structure used by DESNZ.

### **Step 1: Identifying the policy objective, ensuring it addresses a market failure or equity concern, and determining whether a subsidy is the right tool to use**

2.2 Under Step 1, public authorities should consider compliance of a subsidy with:

- (a) Principle A: Subsidies should pursue a specific policy objective in order to remedy an identified market failure or address an equity rationale (such as local or regional disadvantage, social difficulties or distributional concerns); and
- (b) Principle E: Subsidies should be an appropriate policy instrument for achieving their specific policy objective and that objective cannot be achieved through other, less distortive, means.<sup>14</sup>

### **Policy objectives**

2.3 The Assessment states that the policy objective of the GHNF Scheme is to incentivise heat network market transition to low-carbon heat sources via targeted financial support, that will help stimulate the increased deployment of low-carbon technologies at scale.

2.4 The Assessment sets out a number of the GHNF Scheme's sub-objectives underpinning this, which are to:

- (a) Achieve carbon savings and decreases in carbon intensity of heat supplied (an estimated 13.9 MTCO<sub>2</sub>e (Million Metric Tons of Carbon Dioxide Equivalent) carbon savings by 2050);
- (b) Increase the total amount of low-carbon heat utilisation in retrofitted and new heat networks (an estimated 2.36 terawatt-hours (TWh) of low-carbon heat per year by 2033); and
- (c) Contribute towards market transformations across the investment landscape and supply chain that will better prepare the heat network sector for further decarbonisation (with the aim to achieve an average of 71%+ external funding leveraged by Scheme closure).

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<sup>14</sup> See [Statutory Guidance](#), paragraphs 3.33–3.59 and the [SAU Guidance](#), paragraphs 3.6–3.10 for further detail.

- 2.5 The Assessment outlines the wider policy context for heat networks. It notes the Committee on Climate Change’s view that heat networks are essential to a least cost net zero pathway, requiring £5.5 billion of government investment by 2030 to unlock a further £12 billion of private capital.<sup>15</sup> The Assessment also highlights recent UK Government emphasis in the Warm Homes Plan which identifies that around 20% of UK heat demand could be most effectively met through heat networks, up from 3% currently.<sup>16</sup> It outlines that an interim target is being set for heat networks to supply 7% of UK heat by 2035.
- 2.6 In our view, the Assessment clearly describes and evidences the specific policy objective of the GHNF Scheme and how it relates to wider government objectives regarding heat networks.

### **Market failure**

- 2.7 Market failures arise where market forces alone do not produce an efficient outcome. When this arises, businesses may make investments that are financially rational for themselves, but not socially desirable.<sup>17</sup>
- 2.8 The Assessment describes the following market failures which it considers lead to a lower level of deployment of low-carbon heat networks than is socially optimal:
- (a) Externalities: The Assessment states that most buildings and existing heat networks are heated by fossil fuels, and that the full costs imposed on others due to greenhouse gas emissions are not accounted for. It explains that the GHNF Scheme will overcome this market failure by allowing low-carbon heat networks to achieve cost competitiveness with alternative technologies such as gas networks and smaller heat pumps where heat networks are a socially optimal solution.
  - (b) Imperfect information: The Assessment explains that uncertainty about the delivery, costs and demand for low-carbon heat networks leads investors to perceive them as higher risk and often expect higher returns on investment. It argues that the GHNF Scheme will overcome this market failure by increasing consumer confidence and understanding, reducing risk for investors, and increasing the capability and capacity of the supply chain.
- 2.9 In our view, the Assessment clearly describes the market failures that the GHNF Scheme seeks to remedy. However, while it provides a credible description of the market failures and how the GHNF Scheme will address them, the Assessment could evidence in more detail the existence of these market failures and explain

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<sup>15</sup> [Research on district heating and local approaches to heat decarbonisation \(Element Energy\) - Climate Change Committee.](#)

<sup>16</sup> See Chapter 5, [Warm Homes Plan – GOV.UK.](#)

<sup>17</sup> [Statutory Guidance](#), paragraphs 3.36–3.51.

how they lead to under-provision of low-carbon heat networks compared to fossil fuel heat networks. For example, it could set out the cost differential between fossil fuel and low-carbon heat networks.

## Appropriateness

- 2.10 Public authorities must determine whether a subsidy is the most appropriate instrument for achieving the policy objective. As part of this, they should consider other ways of addressing the market failure or equity issue.<sup>18</sup>
- 2.11 The Assessment acknowledges that the GHNF Scheme is one part of a wider Heat Networks Transformation Programme which includes:
- (a) regulation and consumer protection, such as making Ofgem the regulator for heat networks;
  - (b) support for supply chain skills through training grants;
  - (c) support for efficiency improvements to existing networks;
  - (d) mandatory improvements to technical standards for heat networks; and
  - (e) granting new powers to local government to designate areas as heat network zones in England, accelerating heat network development in areas where they are projected to be the most affordable heating solution.
- 2.12 However, the Assessment explains that, given their scale and complexity, the GHNF Scheme will still be key to achieving an increase in deployment of low-carbon networks and leveraging external investment into the market in the medium term.
- 2.13 The Assessment states that DESNZ considered the following options in 2021 before the introduction of the GHNF Scheme to see how well they could enable the delivery of intended policy objectives, using critical success factors to assess strategic fit, value for money potential, market development potential and achievability:
- (a) Do Nothing: Letting the previous Heat Network Investment Project (HNIP)<sup>19</sup> run until its expiry in March 2022 with no further government support provided thereafter.
  - (b) Various capital support programmes: HNIP 2 (grants and loans to heat networks projects with no explicit focus on low-carbon heating), a GHNF focused on existing heat networks only, a GHNF focused on supporting new

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<sup>18</sup> [Statutory Guidance](#), paragraphs 3.57–3.59.

<sup>19</sup> [\[Withdrawn\] Heat Networks Investment Project \(HNIP\): overview - GOV.UK](#).

heat networks only, and a GHNF supporting a balance of new and existing heat networks.

- (c) Bringing forward heat network regulations: Bringing forward plans to implement a low-carbon heat network zoning policy and a market framework to regulate heat networks including a low-carbon emissions standard.

- 2.14 The Assessment sets out that the three GHNF options scored better in terms of strategic fit, value for money, and contribution to market growth outcomes compared to the other options, and that regulation was unfeasible to implement within the expected timeline due to legislation constraints. Therefore, DESNZ deemed HNIP 2 and regulation not to be viable options. The Assessment explains that a GHNF supporting a balance of new and existing heat networks was introduced (and then extended and modified with an increased budget through the GHNF Scheme) as this was judged to have the most impact in terms of meeting the policy objectives and developing low-carbon heat networks and supporting sectors, whilst still offering value for money due to the lower costs involved in decarbonising existing heat networks.
- 2.15 The Assessment states that the 2021 appraisal is still considered valid, and that this is supported by evidence of the effectiveness of the GHNF to date. Therefore, DESNZ's preferred option is to continue to fund both existing and new build projects through the GHNF Scheme.
- 2.16 In our view, the Assessment demonstrates that DESNZ has considered other ways of achieving its policy objective and explains why a subsidy was the most appropriate option. However, whilst the Assessment clearly describes the GHNF Scheme's role in the wider policy landscape and the options considered when the GHNF was developed in 2021, it should focus on alternatives to subsidy rather than other forms of subsidy and explain why other non-subsidy options (such as commercial loans or equity investments) were not considered appropriate to achieve the policy objective in the current market context.

## **Step 2: Ensuring that the subsidy is designed to create the right incentives for the beneficiary and bring about a change**

- 2.17 Under Step 2, public authorities should consider compliance of a subsidy with:
- (a) Principle C: Subsidies should be designed to bring about a change of economic behaviour of the beneficiary. That change should be something that would not happen without the subsidy and be conducive to achieving its specific policy objective; and

- (b) Principle D: Subsidies should not normally compensate for the costs the beneficiary would have funded in the absence of any subsidy.<sup>20</sup>

## Counterfactual

- 2.18 In assessing the counterfactual, public authorities should consider what would likely happen in the future – over both the long and short term – if no subsidy were awarded (the ‘do nothing’ scenario).<sup>21</sup>
- 2.19 The Assessment sets out that, as both individual and heat network heating systems are currently dominated by high carbon, gas-fired technologies for households and commercial users, it would be difficult to incentivise the transition from gas to low carbon technologies at the pace required absent the GHNF Scheme.
- 2.20 It explains that, as each individual grant award covers only a proportion of total costs, the GHNF Scheme leverages external funding into projects which would otherwise not be deployed on developing or building a low-carbon heat network.
- 2.21 The Assessment explains that the GHNF Scheme is also important in preparing the heat networks sector to meet incoming regulatory requirements relating to decarbonisation and to facilitate heat network zoning. It explains that, without the capital injection offered by the GHNF Scheme, the government’s legislative objectives for the heat network sector would be harder to achieve.
- 2.22 The Assessment sets out that over the medium to long term, the GHNF Scheme will change the way many local communities receive heating by moving them away from fossil fuel sources such as individual or communal gas boilers to heat networks powered by low carbon technologies.
- 2.23 In our view, while the Assessment discusses the potential positive impact of implementing the GHNF Scheme on the adoption of heat networks, it should more clearly explain what would happen in a counterfactual scenario where the GHNF Scheme is not implemented. To do this, the Assessment could explain how the absence of the GHNF Scheme will affect the investment decisions of potential beneficiaries, and their ability to invest at levels necessary to achieve the policy objective. This could be evidenced with analysis of the likely extent of reduced investment in heat networks and/or projects happening on a slower timescale, with regard to a sample of potential beneficiaries, or a sample of beneficiaries from previous funding rounds of the GHNF Scheme.

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<sup>20</sup> See [Statutory Guidance](#), paragraphs 3.60–3.74 and the [SAU Guidance](#), paragraphs 3.11–3.13 for further detail.

<sup>21</sup> [Statutory Guidance](#), paragraphs 3.63–3.65.

## Changes in economic behaviour of the beneficiary and additionality

- 2.24 Subsidies must bring about something that would not have occurred without the subsidy.<sup>22</sup> They should not be used to finance a project or activity that the beneficiary would have undertaken in a similar form, manner, and timeframe without the subsidy ('additionality').<sup>23</sup> For schemes, this means that public authorities should, where possible and reasonable, ensure the GHN Scheme's design can identify in advance and exclude those beneficiaries for which it can be reasonably determined would likely proceed without subsidy.<sup>24</sup>
- 2.25 The Assessment explains that awards are made under the GHN Scheme on the basis that they are assessed to be additional and that the work they are funding would not have gone ahead in the absence of direct grant support. It explains that it is inherent in the design of the GHN Scheme that only heat networks that would not be developed without government support will be supported and sets out situations where funding would not be considered additional.<sup>25</sup>
- 2.26 The Assessment sets out that the GHN Scheme guidance asks applicants to consider whether additionality tests apply which stipulate that any requested award should be restricted to a level that demonstrates additionality. It also explains that applications that pass the core eligibility metrics are given careful assessment by a multi-disciplinary team of experts, who assess techno-economic, commercial, financial and legal aspects of the proposed projects. The Assessment outlines that no credit is given during assessment or funding awarded for elements of a project that do not demonstrate additionality to the satisfaction of DESNZ or the assessors. The Assessment also outlines the eligible costs for the GHN Scheme.<sup>26</sup>
- 2.27 The Assessment explains that the interim evaluation of the GHN Scheme published in December 2025, which covered the first six rounds of funding, found strong qualitative evidence of additionality.<sup>27</sup> It outlines that most GHN Scheme participants interviewed for the evaluation reported that their projects would not have progressed without funding from the GHN Scheme. The Assessment also outlines that those who indicated that they might have been able to progress by other means reported progress would have been slower or projects smaller or less ambitious, had the GHN Scheme not been available.<sup>28</sup>
- 2.28 However, the Assessment outlines that the evaluation also found that there was less evidence that GHN had influenced the type of technology deployed,

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<sup>22</sup> [Statutory Guidance](#), paragraph 3.67.

<sup>23</sup> [Statutory Guidance](#), paragraphs 3.66–3.70.

<sup>24</sup> [Statutory Guidance](#), paragraphs 3.71–3.73.

<sup>25</sup> These situations are outlined in [Green Heat Network Fund \(GHN\): Round 11 application guidance](#), page 16.

<sup>26</sup> See paragraph 1.10.

<sup>27</sup> [Green Heat Network Fund \(GHN\): interim evaluation report](#).

<sup>28</sup> See [Green Heat Network Fund \(GHN\): interim evaluation report](#), pages 34 and 103.

meaning that GHNF did not necessarily incentivise prospective operators of heat networks to switch to low-carbon from high-carbon heat sources.<sup>29</sup>

- 2.29 In our view, the Assessment explains and evidences how the subsidy would change the beneficiaries' economic behaviour and that the GHNF Scheme brings about changes that would not have occurred absent the GHNF Scheme. In particular, the presence of individual project-level tests for additionality and the findings of the interim evaluation clearly supports the Assessment's explanation. It could however further reflect on the findings regarding the GHNF Scheme's ability to change the behaviour of beneficiaries evidenced in the interim evaluation (see paragraph 2.28) and what, if any, implications this has for demonstrating compliance with Principle D.
- 2.30 In addition, while the Assessment has set out the eligible costs the GHNF Scheme will support, when assessing additionality, it should consider whether any of these costs could be considered 'business as usual' costs.<sup>30</sup>

### **Step 3: Considering the distortive impacts that the subsidy may have and keeping them as low as possible**

- 2.31 Under Step 3, public authorities should consider compliance of a subsidy with:
- (a) Principle B: Subsidies should be proportionate to their specific policy objective and limited to what is necessary to achieve it; and
  - (b) Principle F: Subsidies should be designed to achieve their specific policy objective while minimising any negative effects on competition or investment within the United Kingdom.<sup>31</sup>

#### **Proportionality**

- 2.32 The Assessment outlines the caps that limit the size of subsidies under the GHNF Scheme.<sup>32</sup> The Assessment sets out that these are the absolute scheme limits, and that 'most projects are expected to significantly out-perform these to score well in competition'. The Assessment states that no awards will be made where a project's real pre-tax project IRR exceeds the GHNF Scheme maximum support level. It also outlines that projects are required to provide commercial and financial information in support of their applications, such as business cases, techno-economic models, cash flows and accounts.

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<sup>29</sup> See [Green Heat Network Fund \(GHNF\): interim evaluation report](#), pages 36 and 103.

<sup>30</sup> See [Statutory Guidance](#), paragraphs 3.69 and 3.70.

<sup>31</sup> See [Statutory Guidance](#), paragraphs 3.75–3.112 and the [SAU Guidance](#), paragraphs 3.14–3.18 for further detail.

<sup>32</sup> See paragraph 1.11.

- 2.33 Regarding how applicant projects are assessed, the Assessment describes a competitive, multi-stage selection process involving a 'detailed' application form, 'extensive' mandatory supporting evidence, and scoring against gated criteria by a multi-disciplinary assessment team. It explains that projects that meet key requirements undergo a further deliverability assessment and that assessors can make recommendations for partial funding only, if certain costs are not justified. The Assessment outlines that final funding decisions are made by an Investment Committee comprising delivery partner advisers and senior DESNZ voting members, which also takes into account an applicant's potential ability to find funding from other sources. The Assessment outlines that applicants are advised that securing third-party investment to reduce their grant request could significantly improve the competitiveness of their application.
- 2.34 The Assessment explains that funding agreements with beneficiaries include clawback provisions covering project cessation, unsatisfactory progress, and breach of the maximum carbon intensity criteria. It outlines that funds may also be withheld or clawed back where a recipient is found to have misrepresented their financial position, including by failing to declare other subsidies received.
- 2.35 The Assessment also sets out that projects might receive subsidy from other sources such as central or local government funding schemes. It outlines that applicants are required to confirm whether other sources of public funding, either awarded or applied for, are included in the financial model submitted as part of their applications and that DESNZ also carries out checks to mitigate the likelihood of double-subsidy. The Assessment also outlines that funding agreements require recipients to declare other subsidies, maintain compliance records, and provide legal opinions where other subsidies are received.
- 2.36 The Assessment states that applicants to the GHNF Scheme will be encouraged to seek financing options from the National Wealth Fund (NWF) and can opt in to having their applications shared with the NWF to consider whether the project may be suitable for their range of finance products. The Assessment sets out that the NWF's decisions on whether to offer support to projects (either at market or concessionary rates) are distinct from investment decisions under the GHNF Scheme and are taken according to the NWF's own investment criteria and policies. It sets out that the risk of 'cumulation arising from over-compensation' through this interaction with the NWF is mitigated by 'subsidy control provisions in the funding agreements, coupled with regular contact between DESNZ, our delivery partner and the NWF and the regular monitoring and reporting regime that exists for GHNF funded projects, in which they are required to provide information about their financial position.' For example, supporting evidence provided by DESNZ sets out the requirement for applicants to provide a revised private IRR hurdle rate reflecting the reduction in financial risk resulting from the inclusion of NWF alongside GHNF funding.

- 2.37 The Assessment notes that the options appraisal set out in relation to Principle E (see paragraph 2.13) is also relevant to Principle B as it explored the effectiveness of different means to achieving the GHNF Scheme’s policy objective.
- 2.38 In our view, the Assessment outlines a number of features that contribute to ensuring that the GHNF Scheme is proportionate and limited to what is necessary, in line with the Statutory Guidance. For example, the Assessment advises applicants that reducing their grant request through securing third-party investment could significantly improve the competitiveness of their application. However:
- (a) The Assessment should provide further detail on the financial tests used to verify that the costs of each project do not exceed the minimum necessary. This could include an overview of how costs are challenged by assessors and where appropriate, reduced.
  - (b) The Assessment should explain and evidence in more detail how DESNZ set the caps that limit the size of awards (such as the cap regarding real pre-tax project IRR) and why they are considered to be set at the appropriate level to help demonstrate compliance with Principle B.
  - (c) Given the possibility that projects can receive funding from other public sources, the Assessment should consider how this impacts the assessment of the proportionality of individual awards, particularly in relation to assessing the project against the GHNF Scheme’s financial criteria and funding caps.

### **Design of subsidy to minimise negative effects on competition and investment**

- 2.39 In relation to the nature of the instrument, the Assessment explains that grants are the chosen instruments because they minimise market disruption by retaining healthy competition at the procurement stage, rather than directly providing the support to contractors. It explains that, through the market transformation commitments<sup>33</sup> that recipients must sign, beneficiaries must undertake to use open procurement and DESNZ intends to encourage open information sharing concerning projects across the industry, wider supply chain participation, new market entrants, and open competition and greater private investment.
- 2.40 The Assessment explains that a set of gated eligibility criteria screen out projects that do not meet the GHNF Scheme’s objectives.<sup>34</sup> Regarding consumer detriment, the Assessment explains that, where heat network users are domestic customers or micro-businesses, applicants must demonstrate that the proposed levelized tariffs must be lower than the low-carbon heating counterfactual for new buildings or the gas/oil counterfactual for existing buildings.

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<sup>33</sup> [Annex 3: GHNF market transformation commitment.](#)

<sup>34</sup> See paragraph 1.9.

- 2.41 The Assessment explains that, unlike its predecessor (HNIP), the GHNF Scheme does not offer loans alongside grants, with loan funding responsibility shifted to private and institutional investors and the NWF. It sets out that the deliverability assessment of proposed projects combined with monitoring and reporting requirements are designed to preserve the financial rigour and discipline that loan funding would otherwise have provided.
- 2.42 The Assessment explains that the drawdown of grant funding is linked to milestones and that these differ depending on whether the grant recipient is a local authority or other body. It outlines that local authorities can claim their funding in one tranche if all conditions precedent attached to the funding award have been met and non-local authorities are required to draw down funds in arrears of evidenced spend, with funding also ringfenced to eligible costs for the specific applicant and project.
- 2.43 The Assessment describes the monthly monitoring and reporting requirements placed on beneficiaries during the commercialisation and construction phases. It explains that funds are claimed from the GHNF Scheme through these monthly reports, and that failure to submit these reports results in no payments being made. The Assessment outlines that, once operational, quarterly operational data will be provided to DESNZ to evidence the longer-term benefits. The Assessment explains that the GHNF Scheme itself is also subject to evaluation, undertaken by third parties, and that the interim evaluation published in December 2025 covered the first six rounds.
- 2.44 In our view, the Assessment clearly demonstrates and evidences how design features of the GHNF Scheme contribute to minimising any negative effects of the GHNF Scheme on competition and investment within the United Kingdom. However, the Assessment could explain any scope for the terms of the Scheme to promote fair pricing by the relevant heat network operators, drawing on an assessment of the regulatory provisions which apply in the market (see paragraph 2.49).

### **Assessment of effects on competition or investment**

- 2.45 Within Step 4, the Assessment discusses the impacts of the GHNF Scheme on competition and investment, covering upstream and downstream markets and geographic effects. The Assessment sets out that the GHNF Scheme is demand-led and open to applicants across England<sup>35</sup> regardless of location, with past awards centred mainly on London, Yorkshire and the Humber, and the South-West with other regions such as the East and West Midlands, and the North-West also benefitting.

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<sup>35</sup> The GHNF is now open to applicants from Wales also - see footnote 7.

- 2.46 The Assessment identifies the relevant upstream and downstream markets. On the upstream side, it identifies increased demand for raw materials used in steel and polymer piping as the main impact, noting that some projects have been affected by price fluctuations linked to events such as the war in Ukraine. On the downstream side, it identifies markets for large heat pumps, heat recovery units and HIUs as the primary affected markets. The Assessment notes that large heat pumps are often imported from Europe, particularly Scandinavia and Germany, while HIUs have significant UK production and design activity.
- 2.47 In relation to competition and investment, the Assessment explains that the GHNF Scheme is specifically intended to shift producers and consumers of heat away from fossil fuels towards low-carbon alternatives such as large-scale heat pumps, geothermal energy, recovered heat and energy from waste. It acknowledges that this will affect the market for gas boilers and fossil fuel technologies, but notes that moving away from these technologies is part of the GHNF Scheme's objective. The impact on those markets is expected to be marginal in the short to medium term given that heat delivered through the GHNF Scheme represents less than 1% of England's heat demand and that beneficiaries are typically local authorities and heat network specialists rather than investors in competing markets. The Assessment also acknowledges that, since many supported heat networks use large-scale heat pumps, the GHNF Scheme may affect the balance of sales between large and small heat pumps. The Assessment notes that this impact cannot be quantified, but that it may be offset by the Boiler Upgrade Scheme,<sup>36</sup> which supports smaller domestic heat pump deployment.
- 2.48 In our view, the Assessment considers and evidences effects of the GHNF Scheme on competition and investment, in line with Annex 3 of the Statutory Guidance. For example, the Assessment provides a useful analysis of some upstream and downstream market effects and investment distortions. However, to better demonstrate compliance with Principle F, the Assessment could set out a more systematic assessment of distortions to competition and investment under Step 3.
- 2.49 In addition, the Assessment should consider in more detail the competitive outcomes expected in the market for the supply of heat as a result of the Scheme. As part of this, it should consider the nature of competition in the markets for the supply of heat through heat networks, noting that these can exhibit the features of natural monopolies (ie each network becomes the sole supplier within their service area and do not compete with other heat networks for customers).<sup>37</sup> As part of this

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<sup>36</sup> Through the Boiler Upgrade Scheme, domestic consumers can get a grant to cover part of the cost of replacing fossil fuel heating systems with a heat pump or biomass boiler - [Apply for the Boiler Upgrade Scheme: Overview - GOV.UK](#).

<sup>37</sup> See [CMA's heat networks market study \(2018\)](#).

assessment, it could also consider any relevant regulatory provisions in this market (see paragraph 2.44).

#### **Step 4: Carrying out the balancing exercise**

- 2.50 Under step 4 (principle G), public authorities should establish that the benefits of the subsidy (in relation to the specific policy objective) outweigh its negative effects, in particular negative effects on competition or investment within the United Kingdom and on international trade or investment.<sup>38</sup>
- 2.51 The Assessment reiterates the three sub-objectives of the GHNF Scheme and the outcomes these will achieve, as set out in paragraph 2.4 above.
- 2.52 The Assessment explains that the benefits achieved by the GHNF Scheme will only be more fully measurable when completed networks are operational, with only three out of 48 funded networks having started supplying heat so far and none having fully completed construction.
- 2.53 Having said this, as well as outlining the findings discussed at paragraph 2.27 above, the Assessment states that the interim evaluation of the GHNF Scheme shows that:
- (a) Grant funding was essential for making projects viable and overcoming market barriers, and that most projects would not have progressed without funding due to the greater cost of low-carbon technologies compared to high.
  - (b) On average, projected IRR rose from 2.8% pre-GHNF to 8.1% post-grant funding, demonstrating that the GHNF Scheme has improved the attractiveness of heat network projects for investors.
  - (c) The availability of funding was an incentive to move forward more quickly with projects than otherwise planned.
  - (d) The GHNF Scheme improved financial viability such that organisations could overcome hurdle rates, the risk of cash flow difficulties were reduced, and grant funding could be spent on the early-stage, higher risk infrastructure investments (subsequently unlocking additional finance).
  - (e) In multiple cases, the GHNF Scheme enabled ‘better’ and more strategic networks to apply such as projects using a lower carbon technology, larger networks, or where the lead organisation retained control of the asset or developed a project in collaboration with other project partners.

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<sup>38</sup> See [Statutory Guidance](#), paragraphs 3.113–3.121 and the [SAU Guidance](#), paragraphs 3.19–3.21 for further detail.

- 2.54 The Assessment explains that the GHNF Scheme benefits customers and consumers by generating significant fuel cost savings, for both existing and new build projects, particularly where heat networks recover industrial heat. It outlines that this is ensured by scheme applicants being required to commit to a specified, reasonable heat tariff for their customers.<sup>39</sup>
- 2.55 As explained at paragraphs 2.45 to 2.47 above, the Assessment considers i) the geographical impacts, ii) the potential effects on competition, trade and investment, and iii) the impacts on upstream and downstream markets which the GHNF Scheme will have, and explains why any negative effects are limited. The Assessment concludes that any possible negative impacts around opportunity costs from the GHNF Scheme will be outweighed by the benefits in enabling greater delivery of low-carbon heat and providing investors with confidence to support heat networks.
- 2.56 In our view, the Assessment clearly sets out the positive effects of the GHNF Scheme in relation to the policy objective as well as potential negative impacts, and conducts a balancing exercise between them in line with the Statutory Guidance.
- 2.57 However, to the extent that DESNZ makes changes to its assessment in Step 3, on the basis of this report, it should reflect these in the balancing exercise of Step 4.

## **Energy and Environment Principles**

- 2.58 This section sets out our evaluation of the Assessment against the energy and environment principles.<sup>40</sup>
- 2.59 DESNZ has conducted an assessment of the GHNF Scheme against Principles A and B. We have not identified any other principle that should have been addressed as part of the assessment.

### **Principle A: Aim of subsidies in relation to energy and environment**

- 2.60 Subsidies in relation to energy or the environment should be aimed at (1) delivering a secure, affordable and sustainable energy system and a well-functioning and competitive energy market, or (2) increasing the level of environmental protection compared to the level that would be achieved in the

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<sup>39</sup> This tariff must not exceed the cost which domestic or microbusiness customers would have otherwise paid, on average, with Ofgem-regulated pricing standards being introduced from early 2027.

<sup>40</sup> See Schedule 2 to the Act, and [Statutory Guidance](#), Chapter 4.

absence of the subsidy. If a subsidy is in relation to both energy and environment, it should meet both limbs.<sup>41</sup>

- 2.61 DESNZ set out to us how the GHNF Scheme complies with both the energy and environment limbs of this principle.
- 2.62 The Assessment explains that the GHNF Scheme complies with the energy limb because it is consistent with delivering a secure, affordable and sustainable energy system. DESNZ told us that the GHNF Scheme is targeted at helping to move consumers to more sustainable heat sources with a lower carbon intensity than that of the fossil fuel-led systems mainly in use currently. DESNZ also explained that applicants to the GHNF Scheme are made aware of the need to comply with existing and impending service, regulatory and technical standards for heat networks.<sup>42</sup>
- 2.63 In relation to the environment limb, DESNZ also told us that a social IRR calculation is performed by each project within the application form. DESNZ explained that this evaluates the social cost of emissions and air quality impact of the project when compared to a standard counterfactual and that all projects must show a social IRR of 3.5% or higher to demonstrate social value for money in supporting the GHNF Scheme. They also provided a sample funding agreement as supporting evidence which sets out environmental requirements placed on grant recipients.
- 2.64 In our view, the Assessment clearly explains and evidences how the GHNF Scheme complies with both the energy and environmental elements of Principle A of the Energy and Environment Principles.

### **Principle B: Beneficiary's liabilities as a polluter**

- 2.65 Subsidies in relation to energy or the environment should not relieve the beneficiary from liabilities arising from its responsibilities as a polluter under the law of England and Wales, Scotland, or Northern Ireland.<sup>43</sup>
- 2.66 The Assessment states that the GHNF Scheme complies with this principle, as no applicants to the GHNF Scheme will be relieved from such liabilities as a result of the GHNF Scheme. It explains that funding agreements will include environmental provisions relating to conservation of energy, water and other resources, the minimisation of greenhouse gas and fuel emissions and other pollutants and the promotion of the use of recycled products.

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<sup>41</sup> [Statutory Guidance](#), paragraphs 4.19–4.28.

<sup>42</sup> See [Green Heat Network Fund \(GHNF\): Round 11 application guidance](#) page 48 and pages 128 to 131 for further information.

<sup>43</sup> [Statutory Guidance](#), paragraphs 4.29–4.34.

2.67 In our view, the Assessment clearly explains and evidences how the GHNH Scheme complies with Principle B of the Energy and Environment Principles.

### **Other Requirements of the Act**

2.68 DESNZ confirmed that no other requirements or prohibitions set out in Chapter 2 of Part 2 of the Act apply to the GHNH Scheme.

**10 April 2026**