utilita

# Fairer energy

## The case for energy market reform

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# What's in an energy bill?

It's not as simple as the cost of energy.

Energy bills are made up of **multiple components** covering the costs of the whole energy system – not just for generation, distribution and supply, but also the costs of government policy.

Where those costs sit, and who pays them, has a direct impact on household bills. Making energy fairer starts with getting that balance right.

# Where does £10 go?

## Energy costs

This is the wholesale cost of the electricity and gas that suppliers buy to serve their customers.

## Network costs

The charges paid to gas and electricity networks for building, maintaining and operating the infrastructure that transports energy around the grid.

## Operating costs

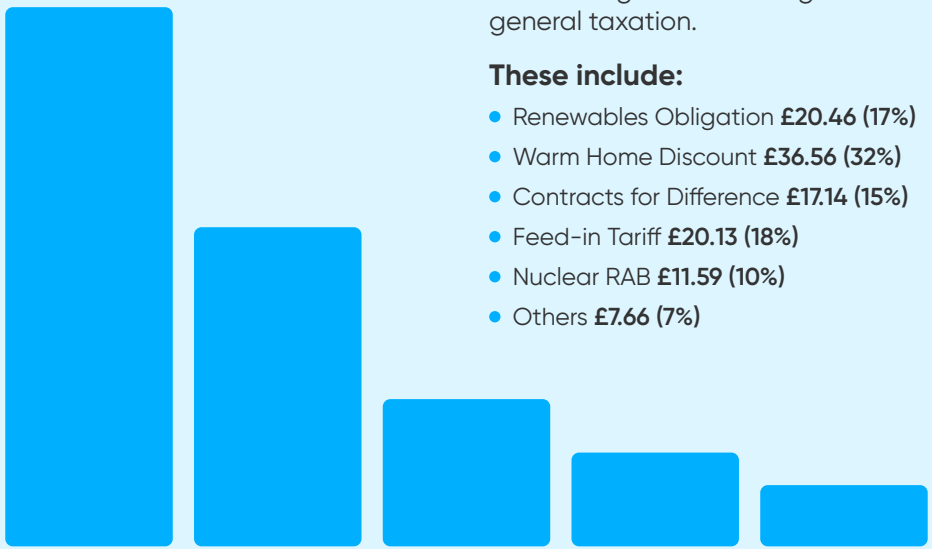
The costs of running an energy supplier, including delivering government policy and schemes, billing and payments, sales and marketing, customer services and metering.

## Policy costs

The cost of government schemes that energy suppliers are required to collect funding for through customer bills, rather than these being funded through general taxation.

**These include:**

- Renewables Obligation **£20.46 (17%)**
- Warm Home Discount **£36.56 (32%)**
- Contracts for Difference **£17.14 (15%)**
- Feed-in Tariff **£20.13 (18%)**
- Nuclear RAB **£11.59 (10%)**
- Others **£7.66 (7%)**



| £4.64 | £2.43 | £1.15 | £0.66 | £0.24 |
|---|---|---|---|---|
| Energy | Network | Operation | Policy | VAT |
| £795.28 p.a. | £417.34 p.a. | £197.02 p.a. | £113.53 p.a. | £40.97 p.a. |

## VAT

A 5% tax applied to the energy bill where applicable, which goes to Treasury.

## Debt

Domestic energy debt now stands at around £5 billion. Writing off and recovering that debt, and funding it in the meantime, adds costs to the energy system. Under the price cap, these costs are spread across bills, meaning customers who pay end up subsidising debt elsewhere in the system.

## Supplier margin

Ofgem's price cap includes an allowance for suppliers to make 2.4% EBIT - a measure of profitability. By contrast, network price controls assume 5-7% returns. In reality, suppliers don't achieve 2.4%. Persistent cost underestimation and restrictions on debt recovery mean suppliers have achieved only 13% of that target over the past five years (0.312% EBIT).

## Industry costs

The costs of running industry bodies, including the DCC which manages smart meter communications (the majority of costs), SEGB which runs campaigns on smart meter adoption, and other data services.

## Headroom

An allowance of 1.5% added to other costs to account for uncertainty in Ofgem's modelling and for changes within each cap period.

**There is no single cause of high bills. There are a number of drivers, most of which are outside suppliers' control.**

**Government and the regulator can take action across different areas to support GB households with affordability.**

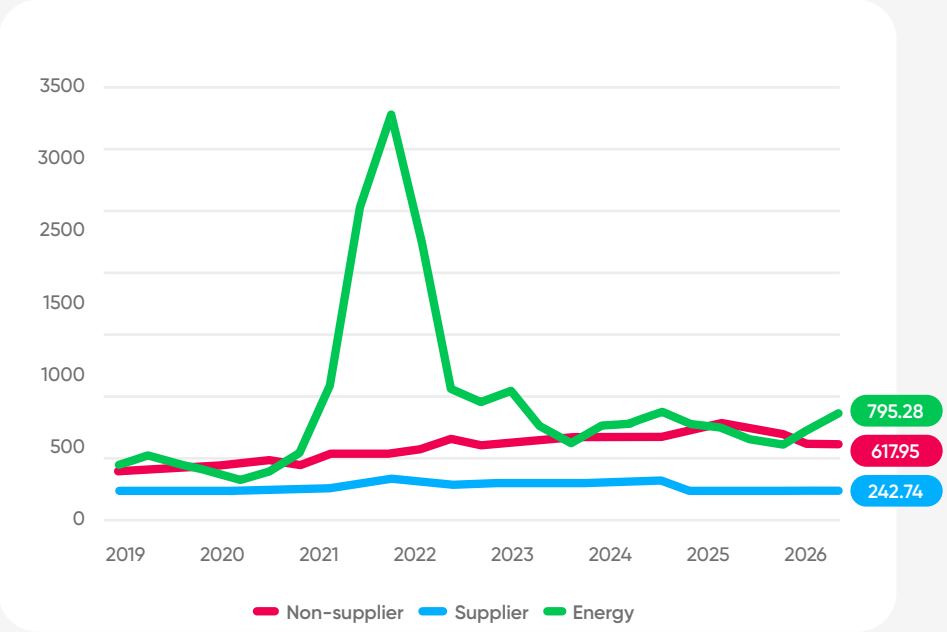
This breakdown uses the October–December 2026 price cap for direct debit customers, given most customers pay by direct debit. The prepayment cap is £45 cheaper at £1,678. Paying by standard credit is the most expensive at £1,861 (£183 more than prepayment). We have included Contracts for Difference (CfD) costs as a policy cost given they are a regulated, government-backed adjustment to the wholesale market price.

| £0.30 | £0.27 | £0.21 | £0.11 |
|---|---|---|---|
| Debt | Supplier margin | Industry | Headroom |
| £51.79 p.a. | £45.72 p.a. | £35.29 p.a. | £18.13 p.a. |

# Even when wholesale prices are stable, structural costs are rising

## Wholesale prices are only part of the picture

Wholesale costs have fallen from the peaks of the energy crisis, but bills remain high. Global events can still cause volatility and Government has limited control over wholesale prices in the short term. It can, however, act on the structural costs that make up a growing share of household bills.

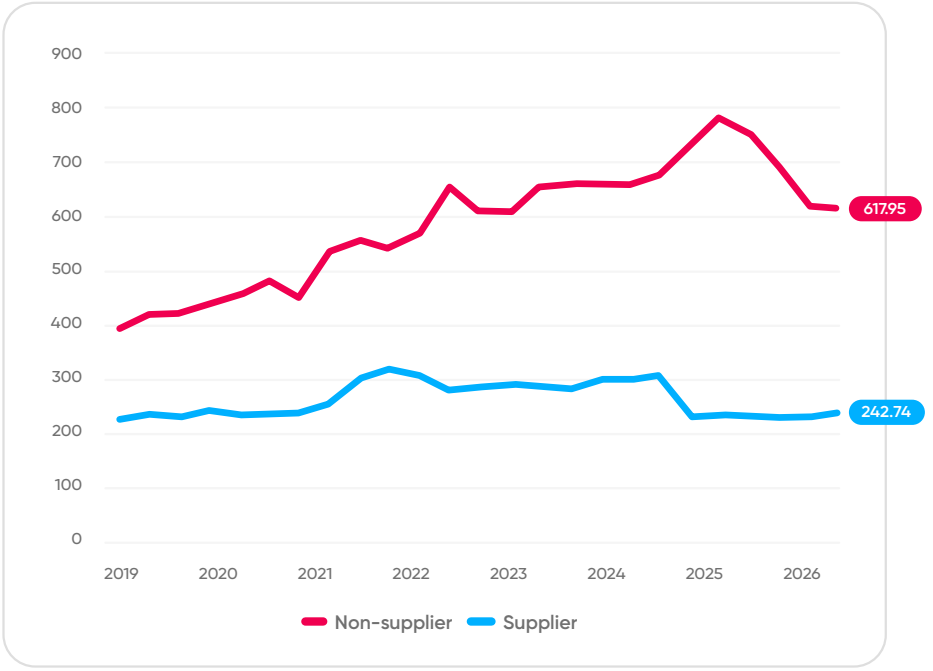



Due to the way the price cap is calculated, supplier costs include actual supplier costs (operating costs and EBIT) in addition to industry costs. Non-supplier costs cover policy, network, industry and debt costs. Energy is the wholesale energy costs. Headroom and VAT are not included.

## Structural costs are rising

Non-supplier costs (including network, policy and bad debt costs) contribute almost as much to a bill as the cost of energy. These costs are projected to continue to increase as we build out energy infrastructure needed to deliver a secure, resilient and low-carbon energy system for the long term. Ofgem estimates network build-out will add £108 to bills by 2031.

Meanwhile, supplier costs have remained relatively stable.

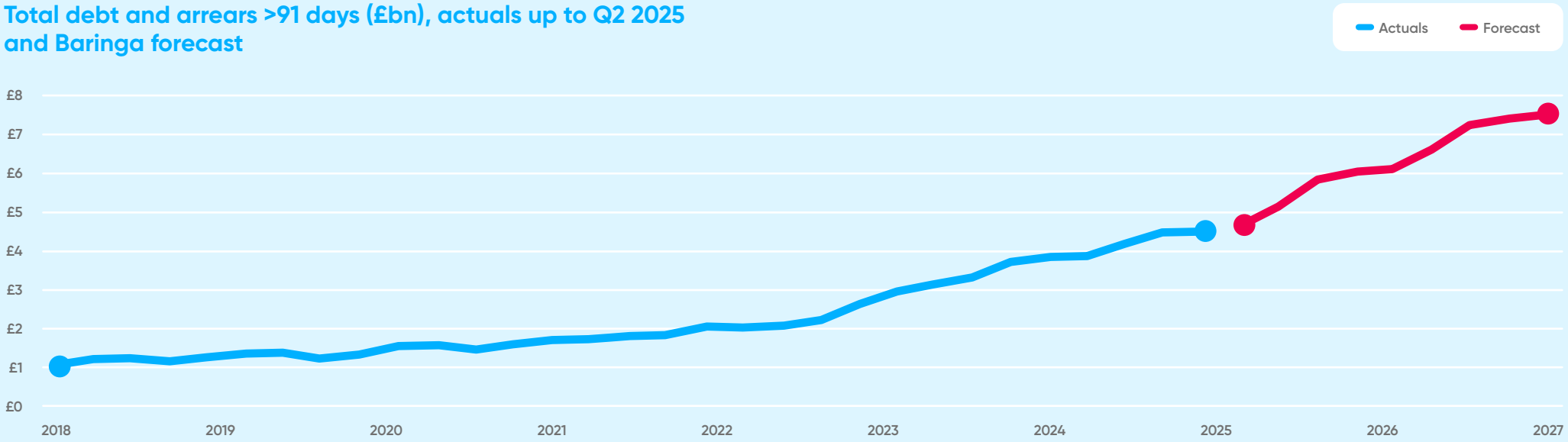



The fall in non-supplier costs shown in 2026 reflects the transfer of the Energy Company Obligation and 75% of the Renewables Obligation from bills into general taxation, lowering annual bills by £149.51 at the time. From July 2026, Ofgem also reduced its 'typical domestic consumption values' to reflect improved energy efficiency. This makes the reduction in structural costs appear greater than the underlying change.

Supplier costs include operating costs, industry costs and EBIT. Non-supplier costs cover policy, network, industry and debt costs. Energy costs are wholesale energy costs. Headroom and VAT are not included.

# Meanwhile, debt is spiralling

## Total debt and arrears >91 days (£bn), actuals up to Q2 2025 and Baringa forecast




There is a misconception that the energy crisis is to blame for the enormous debt burden. However, debt has continued to rise after prices stabilised. Debt is a result of the broader affordability crisis and policy decisions which have limited the ability of suppliers to collect payments.

As suppliers effectively collect money on behalf of other organisations, they take on all the debt risk in the energy sector. Suppliers are expected to manage this risk on behalf of industry but lack recourse to recover costs. This undermines the financial resilience and investability of the retail market while driving up costs for paying customers.

Under the price cap, the cost of bad debt is recovered through customer bills. This means customers who pay end up subsidising debt elsewhere in the system, adding further pressure to already stretched household budgets.

Ofgem should urgently put the brakes on debt accumulation. This should include using technology such as smart pay as you go energy that can help customers stay in control and prevent debt from building up.

Baringa analysis showing total debt and arrears (>91 days). Actuals shown up to Q2 2025. Onwards is Baringa's forecast.

# What needs to change

We need a fairer way to fund the transition and protect households, while promoting investment and innovation.

## 1 Lowering costs

We need to have an honest conversation about rising energy costs, where they should sit and how they should be managed. Bills will continue to increase. If Government wants to prevent this, these costs must be moved elsewhere. If people cannot afford an essential service like energy, this is a social and economic policy problem that Government must address.

Currently, vulnerable and low-income customers carry a disproportionate share of costs while accessing few of the benefits. A fairer balance and the right support are essential to maintaining public consent for the transition.

### Reform Warm Home Discount into a meaningful social discount scheme

The Warm Home Discount has risen by only £10 in a decade and is no longer enough to make a meaningful difference to fuel poverty. The discount should be expanded, uprated in line with inflation and provided as a lump-sum winter credit, when household need is greatest and the risks of cold, damp homes are highest. Government should define eligibility, using secure data matching across public services to target support according to income or medical need. The reformed discount should be funded outside energy bills, with general taxation the clearest and fairest route. Any alternative levy must be carefully tested to ensure its costs are not passed back to households. This would provide meaningful help to more low-income households and reduce the risk of financial difficulty becoming serious debt.

### Review policy costs and move into general taxation

Removing ECO and RO from bills is welcome, as is the commitment to stronger scrutiny of any new costs.

This framework must be delivered quickly and assess all remaining policy costs, including whether they should move into general taxation - a fairer approach than placing a greater burden on those already struggling.

### Put the brakes on debt accumulation and provide relief for those in need

Energy debt is rising, with costs ultimately shared across all customers.

Tackling this must be a priority through a debt-relief scheme, improved affordability support, and ensuring fair debt collection.

### Fund network upgrades through government bonds

The energy transition is a once-in-a-century economic transformation, comparable to post-war reconstruction or wartime mobilisation.

Government could adopt a similar model to fund this, issuing energy transition bonds to raise long-term capital to fund infrastructure upgrades. Transition bonds would attract institutional and public investors, spreading costs more evenly across society and time, while ensuring the benefits of the transition are shared more fairly and accelerating investment into the UK.

### Make network costs fairer

Investment in the networks is essential to delivering a secure, resilient and low-carbon energy system. But customers should not be expected to fund excessive returns.

Government should examine whether a targeted levy on excess network returns could help fund the social discount. It should also explore whether sovereign-backed Energy Transition Bonds, repaid over a longer period, could spread the cost of new transmission infrastructure more fairly.

## 2 Supporting solar

Behind-the-meter solar and batteries are among the most effective ways to cut energy bills. Adding a 5 kWh battery can raise solar self-consumption to 54%, and Utilita believes this can reach up to 70%.

Expanding on-site generation and storage eases pressure on the grid, reduces the costs of network build-out, and makes electric heating and EVs more affordable. It also shields households from volatile international energy markets. Yet many cannot afford these technologies, meaning they shoulder the costs of the transition without accessing the savings.

### Unleash private investment in social housing

Lower-income households and social tenants should not be locked out of the benefits of solar and storage, where the impact can be the greatest.

Government should work with industry to remove the structural barriers to private investment, including public-sector borrowing rules and outdated regulation that has not kept pace with an evolving market. The priority should be to enable workable commercial models rather than rely on grants alone.

This could allow models such as Social Spark to provide solar and storage without upfront costs for housing providers or costs being passed to tenants.

### Move quickly to offer low and zero interest loans

The Warm Homes Plan's commitment to expanding green finance is welcome, but speed is critical. Delays risk stasis in the market as consumers wait for affordable loans.

*For our in-depth breakdown of all of our solar claims, visit our fully transparent, dedicated claims page here: home.utilita.co.uk/claims

### Direct community benefit funds to solar for low-income households

As Government considers how to share the benefits of new infrastructure with host communities, it should channel community benefit funds into rooftop solar for low-income households – ensuring the transition delivers tangible benefits for everyone.

## 3 Unlocking investment and innovation

Suppliers collect costs for parts of the energy system outside their control, with the only give in the system being suppliers' own costs and margins.

In the last five years, underestimated costs and tight price-cap calculations have caused almost £5bn of under-recovery, leading to underinvestment and stalled innovation. This has weakened balance sheets, reduced service quality, slowed progress on net zero and smart-system goals, and ultimately left customers facing weaker competition, less innovation, and higher systemic risk.

Government and Ofgem recognise the need for a retail market that can attract investment, but action is now required.

### Reform the price cap to reward efficiency and protect paying customers

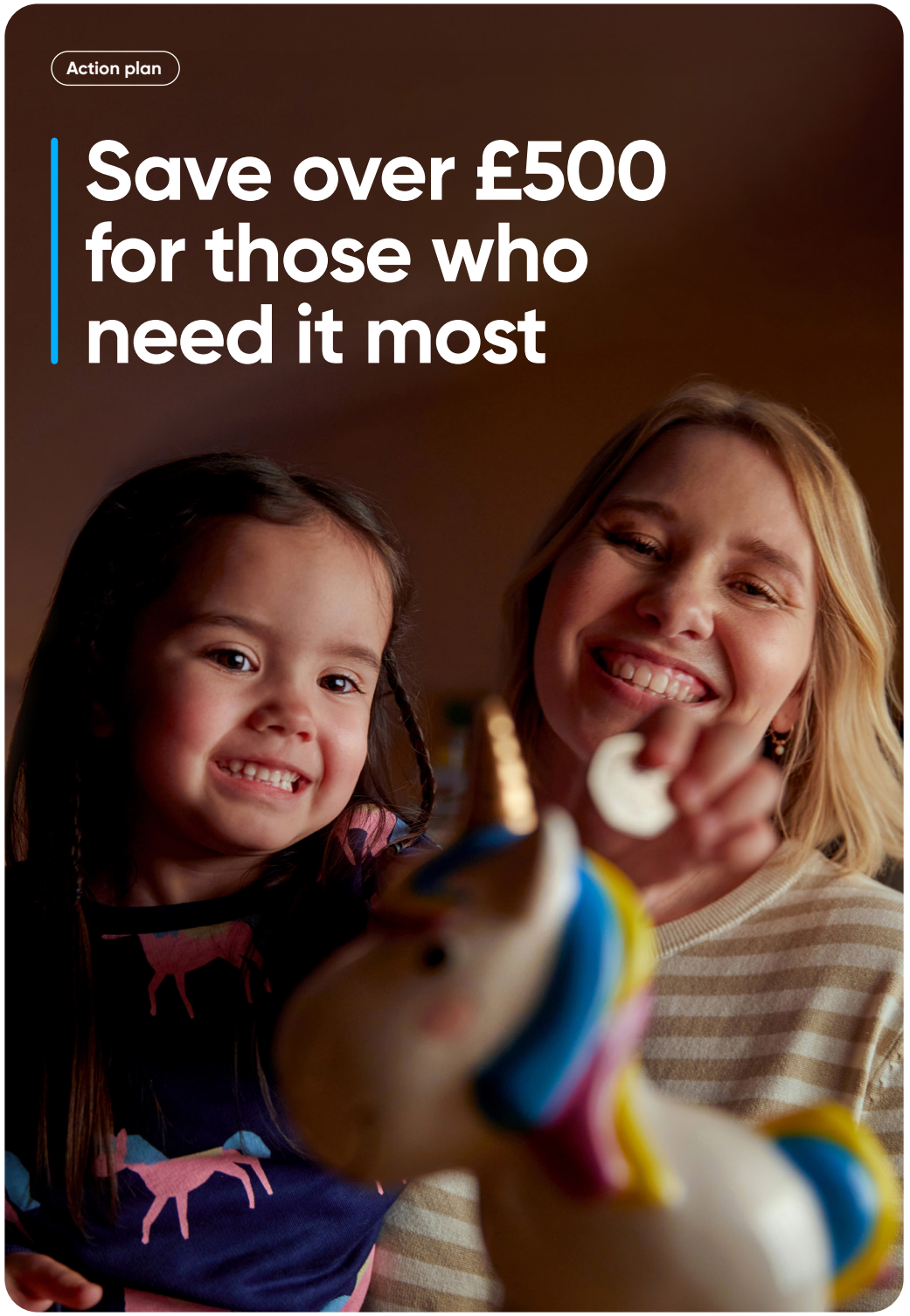
Designed as a ceiling to protect customers from excessive pricing, the price cap has become a pricing target around which suppliers converge. This weakens incentives to reduce costs, trade actively and compete below the cap. The framework also socialises debt costs across bills, requiring customers who pay to subsidise the debt of others. Ofgem should reform the cap to restore incentives for efficiency, while maintaining protection from excessive pricing.

### Streamline retail regulation

Ofgem's supply licence and guidance exceeds 10,000 pages. Much of it is outdated, conflicting or overly prescriptive – it drives up costs, forces convergence, and isn't fit for a future energy system.

An outcomes-based approach, underpinned by guaranteed performance standards and automatic compensation, would set clear minimum expectations while giving suppliers flexibility to innovate. This should be backed by a full review to remove unnecessary rules, with ongoing updates to ensure regulation remains fit for purpose.

# Save over £500 for those who need it most



## An action plan:

- Create a meaningful social discount through expanding the Warm Home Discount, uprating it with inflation and using Government data to target support
- Move quickly to get low and zero interest loans for clean tech on the market
- Remove barriers to private investment in solar and storage for social housing
- Put the brakes on debt accumulation and provide relief for those in need
- Move legacy policy costs off bills and move into general taxation

**Saves up to £90**

- Make network costs fairer by challenging excess returns and exploring longer-term funding options that reduce the pressure of essential investment on today's bills

**Saves £108 by 2031**

- Streamline regulation of the retail market to support innovation
- Direct community benefit funds from renewable projects and infrastructure developers to solar for low-income households
- Reform the price cap to reward efficiency and support innovation

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Version 2.0 - September 2026
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