

# Debt to society update

An updated review of the  
RIIO-2 price controls



**citizens  
advice**

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July 2026

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Please note: all data in this report, unless otherwise stated, is presented on a notional company basis.

# Executive summary

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Last year we reviewed<sup>1</sup> the financial performance of the energy network companies under the regulatory settlements put in place by the energy regulator Ofgem, known as price controls. Our analysis showed that, whilst operational performance was good and associated rewards generally reasonable, the companies had benefited from a windfall resulting from inflation being much higher than expected. That analysis covered up to the end of 2023/4.

Since then, inflation has stayed higher than long-term expectations. This means that the windfall is now around £5bn to the end of 2024/5 and expected to be closer to £6bn by the end of 2025/6. This is clearly beyond any reasonable or legitimate expectations. At the same time, higher inflation has seen people continuing to struggle with the cost of living. Energy debt has continued to rise, now also reaching around £5bn<sup>2</sup>.

And inflation is expected to remain high, and be driven higher, by the current crisis in the Middle East. A consequence of how the last set of price controls were designed means that when inflation is high, companies get overcompensated for their costs of raising debt. Whilst Ofgem has acted to fix the issue going forward, this solution doesn't come in for some of the companies until April 2028. This means for some companies the windfall may build further.

Energy network companies are natural monopolies, people cannot choose their network companies, which is why we have price controls. Price controls are more than a technical regulatory settlement, they represent a social contract. Fair returns on investment, where rewards are earned by genuine outperformance, form part of that social contract. The companies already act to help consumers, including initiatives supporting people in vulnerable circumstances, but to honour that social contract, companies now need to use the windfall to help consumers. Failing to do so, particularly during a cost of living crisis, puts public confidence at risk.

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<sup>1</sup> Citizens Advice, [Debt to Society](#), February 2025

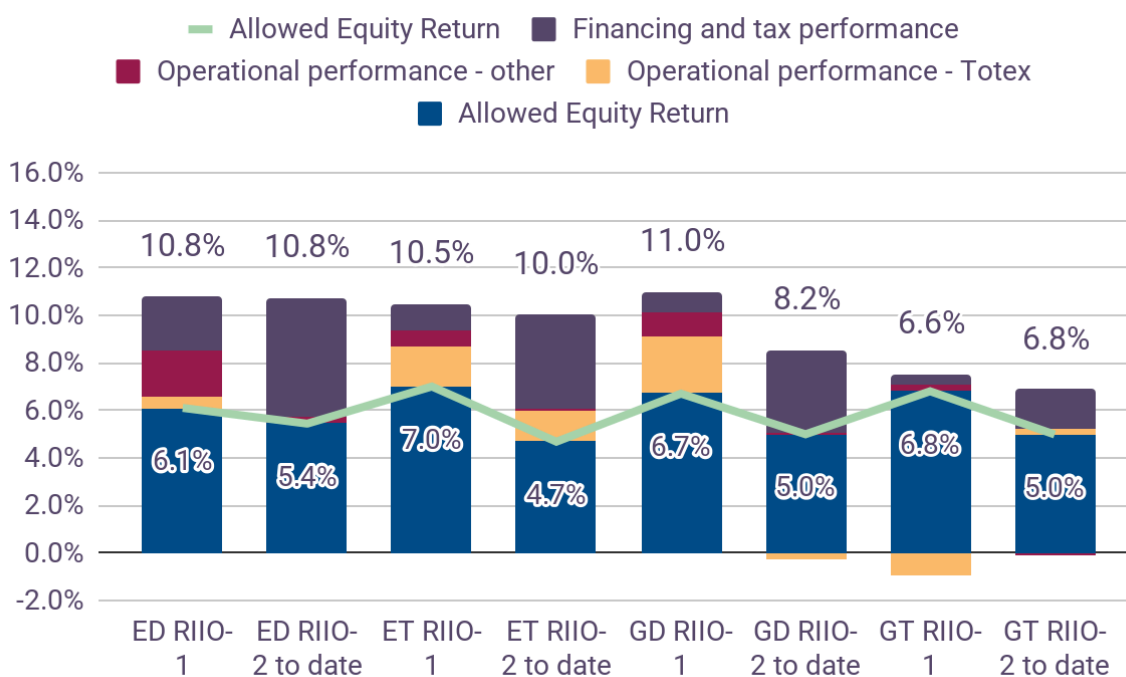
<sup>2</sup> Energy UK, [Energy UK raises alarm over £5.5 billion energy debt crisis](#), February 2026

We're pleased to see Ofgem and the companies looking at how any further windfall can be utilised to benefit consumers. However, we remain of the view that the companies need to take action and make commitments on how the windfall that stretches beyond reasonable and legitimate expectation can be used to support consumers still deep in a cost of living crisis.

## Key findings

Network companies remain able to systematically outperform the level of shareholder returns that Ofgem determined was appropriate (the allowed cost of equity), as shown in Figure 1. Shareholder returns under RIIO-2 continue to remain at the excessive levels seen in RIIO-1, despite Ofgem’s intention to reduce them. Whilst operational outperformance, which largely reflects outcomes for consumers, was the main driver in RIIO-1, debt outperformance drives excess returns in RIIO-2.

**Figure 1: Network companies RoRE<sup>3</sup> performance in RIIO-1 and RIIO-2 to 2025**



The financial outperformance windfall arises when inflation is above the long-run inflation assumption. Last year we reported that networks had made £3.9 billion<sup>4</sup> in excess returns during the first three years of RIIO-2<sup>5</sup> due to

<sup>3</sup> Return in Regulated Equity (RoRE) is Ofgem's measure of the financial return achieved by shareholders from a licensee during a price control period.

<sup>4</sup> In 2023/24 prices

<sup>5</sup> Ofgem's regulatory framework is known as RIIO (Revenue = Incentives + Innovation + Outputs). RIIO-2 ran from

financial outperformance. Since inflation has not yet returned to normal levels, networks have made an additional windfall of **£904 million**<sup>6</sup> in 2024/25. **This makes the total windfall from debt performance to 2025 around £5 billion.**

This windfall arises due to inflation being higher than long-term expectations, which has led to a mis-match between allowances networks are given to cover debt costs and their actual debt costs. An additional £72 million was made from tax outperformance. The combined debt and tax financial performance is mostly not linked to any company performance. They are excess returns that have arisen due to financial arrangements.

After outperforming in their operational performance in the first three years of the price control, the network companies had operational underperformance in 2025 of just over £100 million. The network's total operational outperformance up to 2025 is £664 million. **Total outperformance (financial and operational) in RIIO-2 up to 2024/25 is £5.8 billion.**

Some companies have reported that their performance has been impacted by Real Price Effects (RPEs). These are adjustments made to allowances to reflect changes in network specific input-costs, relative to economy-wide inflation which allowances are linked to. Ofgem uses a proxy for RPEs, and if this proxy is out of line with actual RPEs, companies can over or underspend relative to allowances. However, as is demonstrated in the report, many companies are still spending less than allowances, and for companies that are overspending, the impact on returns is minimal compared to the gains from financial outperformance. This means that overall returns are still above reasonable or legitimate expectations after any RPE effect, although the extent of this excess may have been reduced by RPEs.<sup>7</sup>

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<sup>6</sup> In 2024/25 prices

<sup>7</sup> Ofgem, [Annual report: Electricity Distribution 2024/25](#), p.34

**Figure 2: RIIO-2 operational and financial performance**

<b>£m 24/25</b>	<b>2021/22</b>	<b>2022/23</b>	<b>2023/24</b>	<b>2024/25</b>	<b>Total to 2025</b>
<b>Operational performance</b>	£298	£268	£207	£ -109	£664
<b>Debt performance</b>	£589	£1,378	£2,152	£904	£5,024
<b>Tax performance</b>	£31	£66	£-58	£33	£72
<b>Total performance</b>	£918	£1,712	£2,301	£829	£5,760

The spread of this performance across the four networks is shown in Figures 3 and 4.

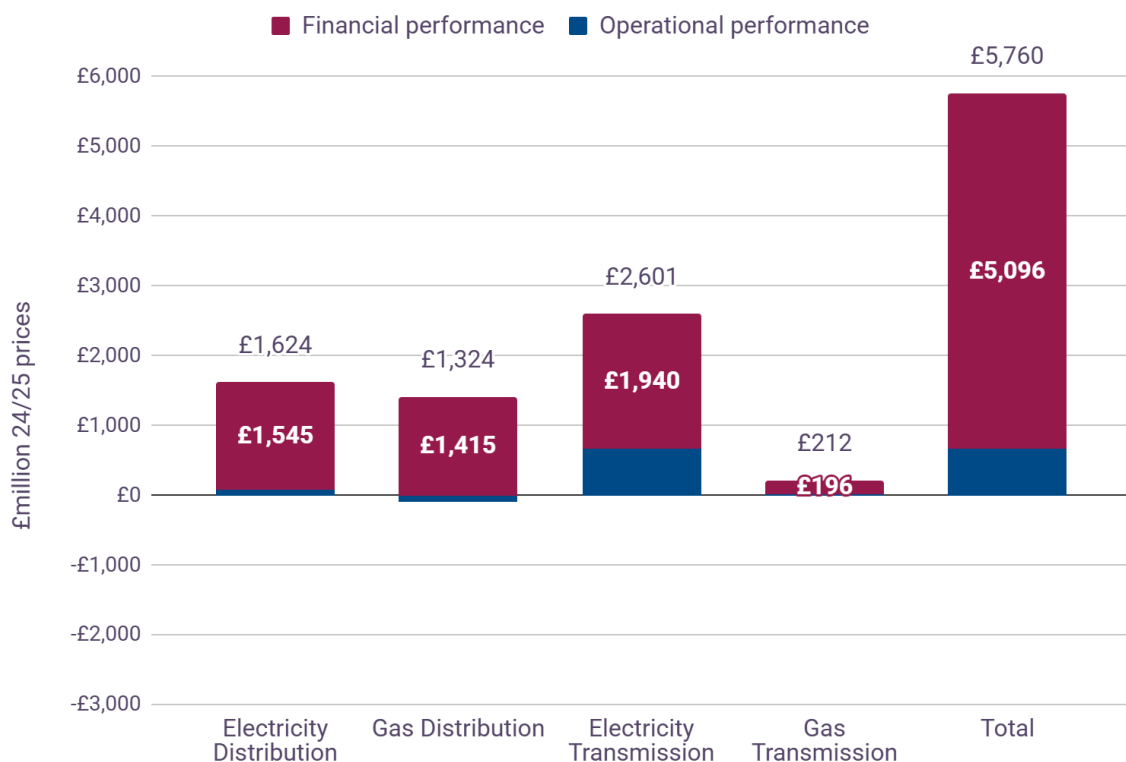
**Figure 3: RIIO-2 sector operational and financial performance**

<b>£m 24/25</b>	<b>Operational performance</b>	<b>Financial and tax performance</b>	<b>Total</b>
<b>Electricity Distribution</b>	£79	£1,545	£1,624
<b>Gas Distribution</b>	- £91	£1,415	£1,324
<b>Electricity Transmission</b>	£660	£1,940	£2,601
<b>Gas Transmission</b>	£16	£196	£212
<b>Total</b>	£664	£5,096	£5,760

Financial and operational RoRE performance is added to the baseline allowed cost of equity set by Ofgem. Real-world evidence suggests that network returns are higher than required by investors. There is a long-list of network companies being acquired at a significant premium. Recent examples include the announcement that Engie will acquire UK Power network companies at a

Market-to-Asset ratio (MAR) of 50%. In August 2024, Iberdrola acquired an 88% stake in Electricity North West (ENWL) at a premium of 60%. In RIIO-3 Draft Determinations Ofgem themselves recognised that ‘it is difficult to accept that large MAR premiums can be justified by assumptions other than higher than required returns or lengthy and consistent expected outperformance’.<sup>8</sup>

**Figure 4: RIIO-2 performance in excess of allowed cost of equity**



The focus of this and the previous report is around the cost of investment made compared to the allowed costs for raising equity. We would like to recognise that the companies undertake lots of activities to support customers, especially those in vulnerable circumstances, that are not covered by this report. This includes through the Vulnerability and Carbon Monoxide Allowance and through the companies’ vulnerability strategies.

<sup>8</sup> Ofgem, [RIIO-3 Draft Determinations - Finance Annex](#), August 2025, p.64.

## Looking forward

Whilst regulatory performance data has only been published up to March 2025, inflation has continued to remain above the long-run assumption since then, particularly due to the Iran crisis. This means networks will be continuing to make a windfall. Using Ofgem's model, based on outturn inflation we have estimated that networks will make a further windfall of around **£838 million** in 2025/2026. This would make the total windfall gained from debt performance in RIIO-2 **almost £6 billion**, to 2026.

**Figure 5: RIIO-2 sector expected debt outperformance to 2026**

<b>£m 24/25</b>	<b>Debt performance to 2025<sup>9</sup></b>	<b>Expected debt performance in 2026<sup>10</sup></b>	<b>Expected debt performance to 2026</b>
<b>Electricity Distribution</b>	£1,545	£376	£1,921
<b>Gas Distribution</b>	£1,415	£239	£1,654
<b>Electricity Transmission</b>	£1,940	£212	£2,152
<b>Gas Transmission</b>	£196	£11	£207
<b>Total</b>	£5,096	£838	£5,934

For electricity transmission, gas transmission and gas distribution 2025/26 is the last year of the RIIO-2 price control. A change has been made in RIIO-3, which commenced this April, to mitigate a windfall arising in this way in the future. However, for electricity distribution, ED2 runs until March 2028, meaning that a windfall will continue arising if inflation remains above the long-run assumption. This is likely, given the impact of the Iran crisis. The Bank of England has published the following CPI inflation scenarios:

<sup>9</sup> In 2025 prices using [2025 RIIO-2 regulatory performance data](#)

<sup>10</sup> In 2025 prices using Ofgem's Open Letter Model

**Figure 6: Bank of England CPI scenarios<sup>11</sup>**

	Scenario A	Scenario B	Scenario C
2026 Q2	3.1%	3.1%	3.6%
2026 Q3	3.3%	3.3%	5.2%
2026 Q4	3.6%	3.7%	6.0%
2027 Q1	3.4%	3.6%	6.2%
<b>Average</b>	<b>3.4%</b>	<b>3.4%</b>	<b>5.3%</b>
2027 Q2	2.9%	3.2%	5.6%
2027 Q3	2.3%	2.8%	4.1%
2027 Q4	1.7%	2.3%	3.5%
2028 Q1	1.4%	2.0%	3.0%
<b>Average</b>	<b>2.1%</b>	<b>2.6%</b>	<b>4.1%</b>

The additional windfall expected in the remaining two years of ED2 ranges from £385 mn to just over £1bn.

**Figure 7: ED2 inflation scenario windfall forecasts**

£m 24/25	2027-2028 windfall <sup>12</sup>	Total windfall across ED2
<b>Scenario A</b>	£385	£2,306
<b>Scenario B</b>	£478	£2,398
<b>Scenario C</b>	£1091	£,3,012

Depending on what happens to inflation in 2027 and 2028, the total windfall for the whole RIIO-2 period is expected to be between **£6.3bn and £7bn**.

<sup>11</sup> Bank of England, [Monetary Policy Report](#), April 2026

<sup>12</sup>In 2025 prices using Ofgem's Open Letter Model

**Figure 8: RIIO-2 sector expected windfall to 2028**

<b>£m 24/25</b>	<b>Expected total RIIO-2 windfall (low inflation)</b>	<b>Expected total RIIO-2 windfall (high inflation)</b>
<b>Electricity Distribution</b>	£2,306	£3,012
<b>Gas Distribution</b>	£1,654	£1,654
<b>Electricity Transmission</b>	£2,152	£2,152
<b>Gas Transmission</b>	£207	£207
<b>Total</b>	<b>£6,319</b>	<b>£7,024</b>

# Key recommendations

## Cost of debt windfall

The way debt allowances have been set in RII0-2 has given network companies a windfall of just over £5bn up to 2025, which is expected to rise to between £6.3bn and £7bn by the time ED2 completes. We believe this is above any reasonable or legitimate expectations of a regulatory settlement. Network companies should demonstrate their commitment to the social contract with consumers.

Last year, we set out some recommendations in response to the windfall. We have continued to review whether direct regulatory intervention to address this windfall would be in the interests of consumers. We recognise that stability and predictability of the regulatory regime provides value to consumers. It will directly impact the cost to consumers of funding the infrastructure required to deliver the energy transition. This means there is a high bar for intervening in a way that could be viewed as retrospective action, although it does not mean that regulatory intervention should always be ruled out. Intervention which undermines this stability has the potential to cause a downgrade in the credit rating of the Ofgem regulatory regime. Any downgrade would generate increased debt costs over the longer term that could outweigh the consumer benefit of recovering the windfall.

It remains that network companies have gained this windfall. We are therefore calling upon network companies to voluntarily use their windfall in excess of reasonable and legitimate expectations in support of consumers. Different companies will be affected differently, depending on the proportion of index-linked debt they hold. It is for the companies to assess how they would like to make best use of their individual windfall, but we would suggest it is appropriate to directly address some of the impacts of the increased energy prices that have contributed to the high inflation that has generated the windfall:

1. Make **voluntary contributions** to the funding required to **provide debt relief for energy consumers**. Ofgem has further consulted on the case for a debt relief scheme to write off debt for low-income households.<sup>13</sup> Previous consultations included exploring an option for suppliers to make direct voluntary contributions to the scheme.<sup>14</sup> This should still be considered and should be extended to network companies.
2. **Facilitate the financing** of any remaining funding requirements for **providing debt relief**. As the £5.8 billion 2025 outperformance is largely a windfall, it should be able to be used without causing any financeability issues for the network companies. Given the size of the windfall we believe the networks should waive any compensation and provide this as the equivalent of an interest-free loan.

In early proposals for the next electricity distribution price control, Ofgem is considering a proposal to utilise the ED2 windfall to reduce notional gearing (the proportion of debt held) which it says ‘will benefit customers by underpinning increased investment and supporting financeability’.<sup>15</sup> We welcome Ofgem considering the windfall and will continue to engage on the issue.

### Getting fairer in ED3

This report shows that during RIIO-1 and RIIO-2 network companies have systematically outperformed the baseline level of return assessed by Ofgem as being appropriate due, in part, to the design of its price controls.

Outperformance to 2025 is £5.8 bn, most of which has not resulted from improved consumer outcomes. Ofgem must ensure that the **returns earned by companies are fairer in ED3** and that reasonable levels of rewards and outperformance are better tied to improved outcomes for customers by:

1. **Removing excess generosity when setting the baseline allowed cost of equity**. Real-world transaction evidence suggests the allowed cost of equity has historically been set too high. It is our view that some of the choices Ofgem makes when setting the baseline return are overly

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<sup>13</sup> Ofgem, [Debt Relief Scheme: Statutory Consultation](#), November 2025

<sup>14</sup> Ofgem, [Resetting the energy debt landscape: the case for a debt relief scheme](#), December 2024

<sup>15</sup> Ofgem, [ED3 Sector Specific Methodology Decision - Finance Annex](#), May 2026, p.6

generous to networks. We explore these issues in the finance section of our response to ED3 SSMC<sup>16</sup> and in our response to the RIIO-3 Statutory Licence conditions consultation.<sup>17</sup>

2. **Ensuring core price control components** like the totex (total expenditure) incentive mechanism are **delivering outcomes consistent with consumer interests** across price controls. Ofgem needs to be explicit about what incentives are for, and what performance would be worthy of reward or penalty. Where incentives are being paid for DNOs to do something which consumers are already paying for, via baseline allowances or otherwise, Ofgem needs to justify this. If it is the case that Ofgem is trying to incentivise DNOs to do something exceptionally well, and better than previously, the incentives should reflect this.
3. **Adopting an Outturn Adjustment Mechanism** in ED3 to prevent systematic over or under performance. This would automatically adjust returns if the median company's RoRE falls outside a reasonable deadband around the baseline allowed cost of equity. We called for this in our response to ED3 SSMC.<sup>18</sup>

## Transparency and reporting

Last year we recommended that Ofgem improve its performance monitoring activity. Ofgem has now published the following RIIO-2 annual reports in January 2026:

- Electricity Distribution<sup>19</sup>
- Electricity Transmission<sup>20</sup>
- Gas Transmission<sup>21</sup>

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<sup>16</sup> Citizens Advice, [response to Ofgem's Sector-Specific Methodology Consultation for ED3](#), December 2025

<sup>17</sup> Citizens Advice, [response to Ofgem's Statutory Consultation on the RIIO-3 Licence Drafting modifications](#), January 2026

<sup>18</sup> Citizens Advice, [response to ED3 Sector Specific Methodology Consultation](#), December 2025, pp.106-107.

<sup>19</sup> Ofgem, [RIIO-2 Electricity Distribution: annual report 2024 to 2025](#), January 2026

<sup>20</sup> Ofgem, [RIIO-2 Electricity Transmission: annual report 2024 to 2025](#), January 2026

<sup>21</sup> Ofgem, [RIIO-2 Gas Transmission: annual report 2024 to 2025](#), January 2026

- Gas Distribution<sup>22</sup>

We welcome this. Ofgem should continue work to make these more accessible and more widely viewed. This is particularly important to ensure reputational incentives are effective.

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<sup>22</sup> Ofgem, [RIIO-2 Gas Distribution: annual report 2024 to 2025](#), January 2026

# Detailed findings

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## Introduction

Great Britain's electricity and gas network infrastructure (transmission and distribution) is owned by monopoly network companies. Due to the high infrastructure requirements of the networks, a competitive market would be inefficient. Instead, Ofgem regulates the prices that network companies can charge through price controls, which are fixed for a period of 5 years. The most recent iteration of the price control was RIIO-2, this ran between 2021/22 and 2025/26 for electricity transmission, gas distribution and gas transmission, and for electricity distribution commenced in 2023/24 and will end in 2027/28. As of April this year, we are now in a new price control period, RIIO-3, for electricity transmission, gas distribution and gas transmission.

The price controls set out how much money can be spent by network companies, what is expected of companies in return for this spending (and what will happen if these expectations are not met), and how much consumers will be charged for this. Whilst previously network charges have made up around a fifth of the average domestic customer's dual fuel energy bill, they now make up over a quarter of the bill. This is due to increasing investment needs in the new price control.

To fund their activities, networks are responsible for securing capital in the form of investment (equity) and borrowing (debt). Just as buying a home has a large up front cost spread over time by a mortgage with interest, consumers also repay capital costs over time. Part of this repayment includes the interest on debt and profit earned by companies to distribute to shareholders in return for their upfront investment.

Network companies have an unambiguous commercial incentive to achieve returns that are as high as possible. The aim of regulation is for the returns companies earn to strike the right balance. It is important for consumers that returns are sufficient so that companies can attract the necessary investment,

without being excessive. Ofgem sets a baseline level of return that it views as appropriate for investors in energy networks. Companies have the opportunity to earn returns above this baseline through incentives which should be conditional upon the best performance.

We have previously shown that realised returns have been excessively high. In our 2019 report *Monopoly Money*<sup>23</sup>, we showed that consumers had overpaid by billions between 2004 and 2019 from Ofgem setting baseline returns too high. In March 2023, our published views<sup>24</sup> on the RIIO-ED2 Final Determinations highlighted that Ofgem's decisions were too generous to company shareholders and cost consumers around £1.5 billion<sup>25</sup> more than was needed. This generosity in setting baseline returns has continued into the current price control, RIIO-3. We explored these issues in our response to the RIIO-3 Draft Determinations consultation<sup>26</sup> and Statutory Licence Modifications consultation<sup>27</sup>.

Ofgem did set out to tighten systematic outperformance in RIIO-2 and our report explores some of the outputs linked to company rewards and penalties. However, due to higher than expected inflation a new problem arose. Financial outperformance, not linked to company outcomes, increased and led to excessive returns.

Our Debt to Society report<sup>28</sup> published last year showed that on top of already high baseline returns, networks have been able to systematically outperform the baseline and achieve excessive returns. During RIIO-1 this resulted from systematic operational outperformance. Whilst this is linked to improved outcomes for consumers, it shows the incentives were too easy to meet leading

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<sup>23</sup> Citizens Advice, [Monopoly Money](#), 2019

<sup>24</sup> Citizens Advice, [Our views on the Ofgem RIIO-ED2 Final Determinations for the electricity distribution sector](#), March 2023

<sup>25</sup> Using Ofgem's own cross-check figures

<sup>26</sup> Citizens Advice, [Citizens Advice responds to RIIO-3 Draft Determinations](#), August 2025, pp.52-70

<sup>27</sup> Citizens Advice, [Advice response to Ofgem's Statutory Consultation on the RIIO-3 Licence Drafting modifications](#), January 2026

<sup>28</sup> Citizens Advice, [Debt to society: what the network companies should do with their windfall profits](#), February 2025

to undeserved high returns. We reported that networks had made £4.5 billion in excess returns in RIIO-2 up to 2024. Of this, £3.9 billion was due to financial outperformance.

Whilst RIIO-2 included a failsafe mechanism against excessive out or under performance, the Return Adjustment Mechanism (RAM), Ofgem took the decision to not include financing costs in the RAM, so as not to expose consumers to either the risks or rewards of company financing decisions. We had previously warned of the risks of excluding financial outperformance from the RAM. Whilst we agree that consumers should not bear the risks of individual companies' financing decisions, the windfall arose from a systemic issue. We believe a well-designed failsafe mechanism should be able to capture this. Ofgem should consider an Outturn Adjustment Mechanism, similar to that applied in the water sector, as an alternative to RAMs.

This report updates the Debt to Society analysis to show that windfall returns from financial outperformance continued in 2024/25. We also analyse operational performance, which looks at the amount networks spend relative to their allowances and their ability to meet outputs, and total network returns, up to 2024/25.

The report uses the latest RIIO-2 regulatory financial performance data<sup>29</sup> which was published in February 2026 and covers RIIO-2 up to and including the financial year 2024/25. For electricity transmission, gas transmission and gas distribution this includes the first four years of RIIO-2, for electricity distribution this includes the first two years of RIIO-ED2. In our Debt to Society report, we called on Ofgem to publish additional performance monitoring commentary in addition to the regulatory performance data. We welcome the sector annual reports covering 2024 to 2025 Ofgem published earlier this year, and call on Ofgem to build upon this.

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<sup>29</sup> Ofgem, [RIIO-2 regulatory performance data: 2025](#)

## Debt outperformance

In our last Debt to Society report we found that the biggest area of outperformance during RIIO-2 to 2024 related to debt costs. These are the costs networks are allowed to recover from consumers to enable them to repay their costs of borrowing. This trend has continued in 2025. We have found that during RIIO-2 to 2025, the amount provided to cover the cost of debt has continued to exceed the actual cost of debt incurred, **by over £5 billion**.<sup>30</sup> It is expected that the windfall will have reached around **£6 bn in 2026**, and is forecast to reach between **£6.3 and £7 bn by the end of RIIO-2/ED2 in 2028**.

The windfall has arisen because of the way debt allowances are calculated in the price control. In RIIO-2, the debt costs networks can recover automatically increase in line with inflation.<sup>31</sup> However, only a portion of debt costs themselves increase inline with outturn inflation (index-linked debt). Some of the actual debt is fixed-rate, so costs do not move in line with inflation, but have an inflation assumption built into the rate. When actual inflation departs from the inbuilt inflation assumption, debt allowances will over or underestimate actual debt costs for the fixed rate portion. The evidence shows that inflation shocks are much more likely to be higher than expected, rather than lower<sup>32</sup>. Since inflation over the past few years has been significantly above the long-run inflation assumption, debt allowances for fixed-rate debt have exceeded actual fixed-rate debt costs.

When setting the debt costs companies can recover, Ofgem's aim is to broadly

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<sup>30</sup> Networks are given a 'real' cost of debt allowance which does not include inflation costs, and earn the inflation part of their debt costs through their Regulated Asset Value (RAV) being indexed in line with inflation. The windfall is made up from the combination of these.

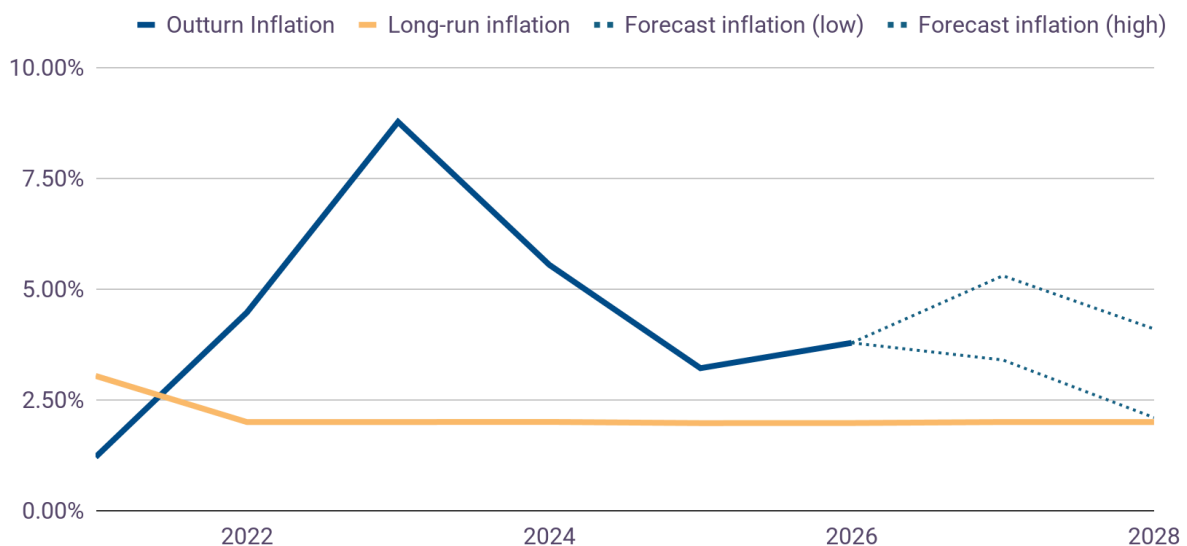
<sup>31</sup> The cost of debt allowance is based on a trailing average of market bond rates, which is then deflated using a long-run inflation assumption (typically 2%). The inflation element of debt allowances is realised through the annual inflation-indexation of the Regulated Asset Value (RAV). We are using the term 'allowance' here to cover both elements.

<sup>32</sup> Ofgem notes that there have been only 5 quarters since 1948 where the RPI YoY change has been below 0% whereas there have been 58 quarters where it was above 8%. [ED3 SSMD - Finance Annex, pp.13-4](#).

match the debt costs networks actually face at a sectoral level.<sup>33</sup> This policy intent has not been achieved, since networks have been allowed to recover debt costs greater than their actual debt costs. Relative to the debt costs companies actually faced, consumers have overpaid. Ofgem has now made changes to how price controls operate to ensure this issue cannot happen again. Had this fix been in place for RII02, the windfall would not have occurred and consumers would be paying less.

Ofgem has stated that this additional return ‘...is a result of an economic sensitivity inherent within the price control and is not associated with business performance or outcomes for the consumer’.<sup>34</sup> This is by definition a windfall.

**Figure 9: Outturn, long-run and forecast inflation<sup>35</sup>**



In practice, the debt outperformance largely accumulates on the Regulated Asset Value (RAV), not paid as instant cash to networks. The RAV is the stock of investment not yet paid for by consumers, and is paid back by consumers

<sup>33</sup> Ofgem aims ‘...to broadly match debt allowances with expected efficient debt costs for RII0-2 through the calibration of the index’. Ofgem: RII0-2 Final Determinations para2.2

<sup>34</sup> Ofgem, [Call For Input - Impact of high inflation on the network price control operation](#), 2023

<sup>35</sup> Outturn inflation is the financial year annual average used in the RII0-2 ET/GDT price control. The longrun assumption is a 10-20 year trailing average. The low inflation forecast is the Bank of England’s [April 2026 Monetary Policy Report](#) scenario A and the high inflation forecast is scenario C.

through depreciation over the regulated asset life (around 20 - 45 years). However, returns which are paid by consumers annually are also inflated as baseline returns are applied to the inflated RAV base. These excess returns and the share of depreciation of the inflated RAV are what consumers pay each year towards this windfall.

The size of debt outperformance will vary by individual company, depending on their financing arrangements. Debt allowances are set on a notional basis, meaning that companies are given an allowance that reflects average debt costs across the sector, rather than individual costs. Companies that have a smaller proportion of fixed-rate debt will have gained a smaller windfall. Only one out of the 14 companies underperformed on debt and tax. Whilst the notional allowance protects consumers from an individual company's financing risks, it does not protect them from systematic overestimation of allowed debt costs.

During 2023, Ofgem consulted<sup>36</sup> on the impact of high inflation on network price controls and the associated increase in real equity returns. In the consultation Ofgem noted that, while these increases may be expected to balance out over time, the current inflationary environment challenged this view. It considered<sup>37</sup>, on balance, that regulatory intervention would not be in the interests of consumers due to any perceived worsening of regulatory stability negatively impacting future investment costs.

Ofgem has made changes to the next set of price controls (RIIO-3) which mean that the outperformance we have seen in RIIO-2 would not reoccur if the inflation conditions were repeated. This represents an acceptance that the increased profits driven by the outperformance are not justified and should be prevented from happening again.

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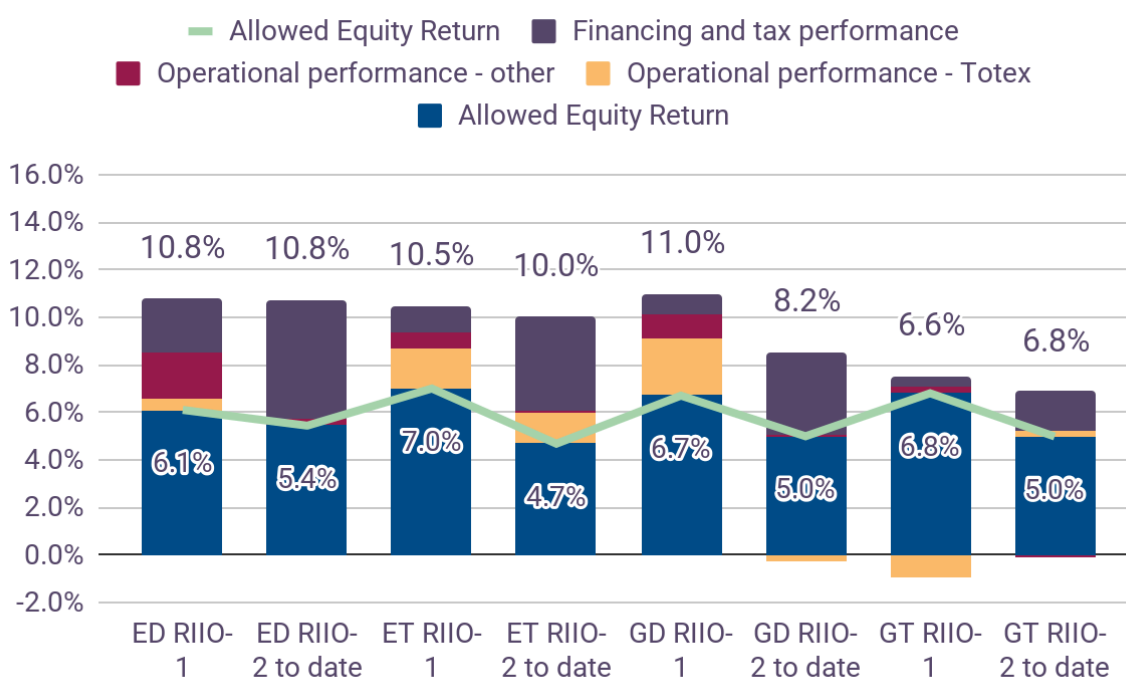
<sup>36</sup> Ofgem, [Call For Input - Impact of high inflation on the network price control operation](#), 2023

<sup>37</sup> Ofgem [Call For Input - Impact of high inflation on the network price control operation – Conclusion and Next Steps](#)

## Network company returns

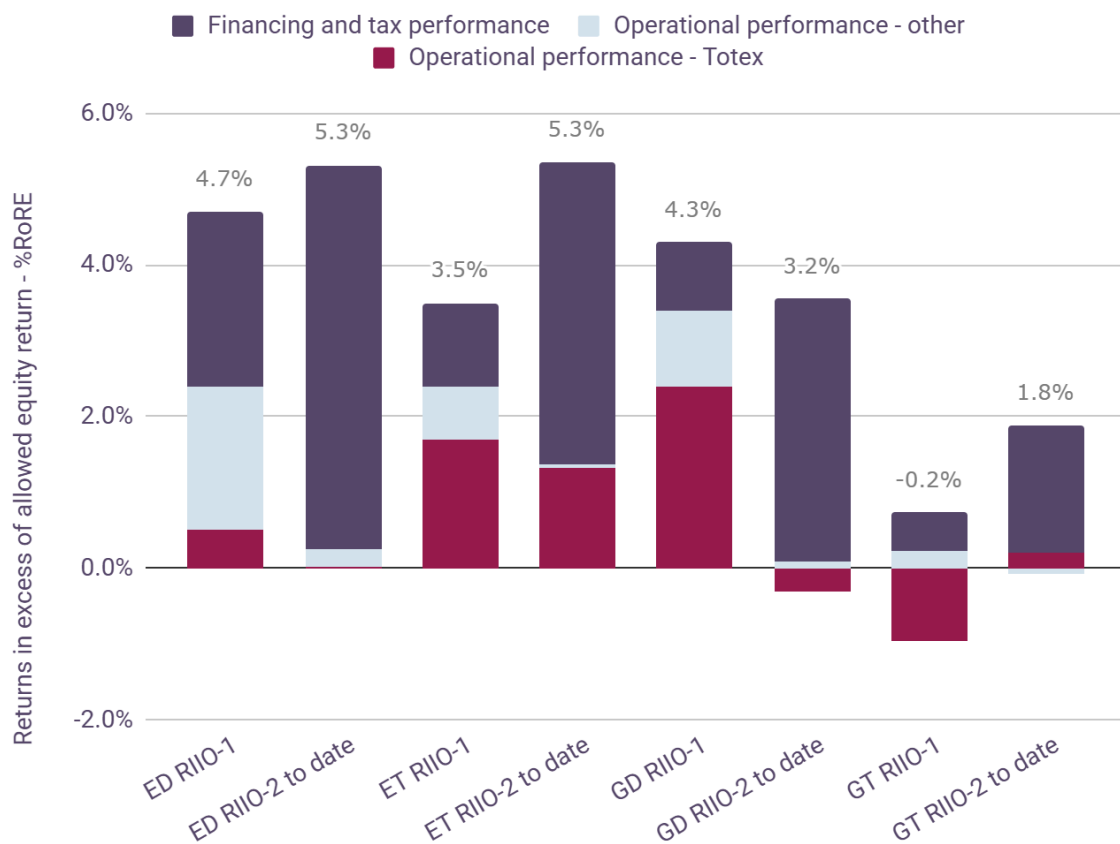
Using Ofgem’s measure of financial performance, known as Return of Regulatory Equity (RoRE), we have found that performance is still at a similar level to the previous set of price controls in contrast to Ofgem’s intent that RIIO-2 would be a tougher price control than RIIO-1.

**Figure 10: network companies RoRE performance in RIIO-1 and RIIO-2 to 2025**



The baseline level of return that Ofgem sees as efficient to attract investment is the allowed cost of equity. Anything above this is additional returns from outperformance against targets. As shown below, excess returns have been greater under RIIO-2 compared to RIIO-1, with the exception of gas distribution which in 2025 turned to below RIIO-1 levels.

**Figure 11: network company returns in excess of allowed equity return - % RoRE**



In contrast to RIIO-1, the main drivers of outperformance in RIIO-2 are overwhelmingly being driven by financing benefits rather than operational factors. Unlike operational factors where benefit is delivered to customers through efficiency or rewards for excellent performance, this financial outperformance has no link with any improved customer outcomes.

Under incentive regulation, companies that perform better than others should be able to earn additional rewards. However, what we observe is systematic overall outperformance with all but one company outperforming their allowed returns and earning additional rewards in RIIO-2, as shown below. Again, we do not see these returns associated with improved outcomes for customers, but because of financing and tax benefits.

**Figure 12: Number of network companies outperforming and underperforming**

Number of companies	RIIO-1		RIIO-2	
	Outperforming	Underperforming	Outperforming	Underperforming
Electricity Distribution	6	0	6	0
Gas Distribution	4	0	3	1
Electricity Transmission	3	0	3	0
Gas Transmission	0	1	1	0
<b>Total</b>	<b>13</b>	<b>1</b>	<b>13</b>	<b>1</b>

Ofgem introduced a failsafe mechanism in RIIO-2 called the Return Adjustment Mechanism (RAM) to tackle situations where returns are unexpectedly too high or too low, however, Ofgem chose not to include financial outperformance within this mechanism so as not to expose consumers to the risks or rewards of company financing decisions. However, this has meant that the debt outperformance windfall has gone uncontrolled in RIIO-2.

### **Enduring Value Adjustments**

The operational performance - totex figures above refer to total expenditure (totex) values with 'enduring value adjustments' applied, where relevant. As part of the regulatory performance data process, networks are allowed to make 'enduring value adjustments' to their reported totex over or under spend values, if they believe that any under or overspend will be offset later in the price control. Ofgem uses these enduring value adjusted totex figures to publish over/underspend as a percentage of annual totex allowance, and subsequent totex RoRE performance. Whilst enduring value adjustments might be useful for long-term economic forecasting, they do not reflect actual spending. We believe it is more transparent for unadjusted totex performance data, reflecting actual

outturn spend, to be published as the default, rather than the adjusted figures. Commentary can then be provided to explain why any adjustment is justified and the adjusted figures presented as supplementary.

## Electricity Transmission

The electricity transmission price control covers the 5 year period between 1<sup>st</sup> April 2021 and 31<sup>st</sup> March 2026. Ofgem's objectives for RIIO-2 were to prepare the network companies to deliver net zero at lowest cost to consumers, while maintaining world-class levels of system reliability and customer service, and ensuring no consumer is left behind.

The RIIO-ET2 price control provided increased funding for load related transmission investment, together with uncertainty mechanisms that could release additional funding if required. Ofgem also introduced measures like Price Control Deliverables (PCDs) to monitor and ensure that investments were delivered. As for returns, the allowed cost of equity was reduced from RIIO-1.

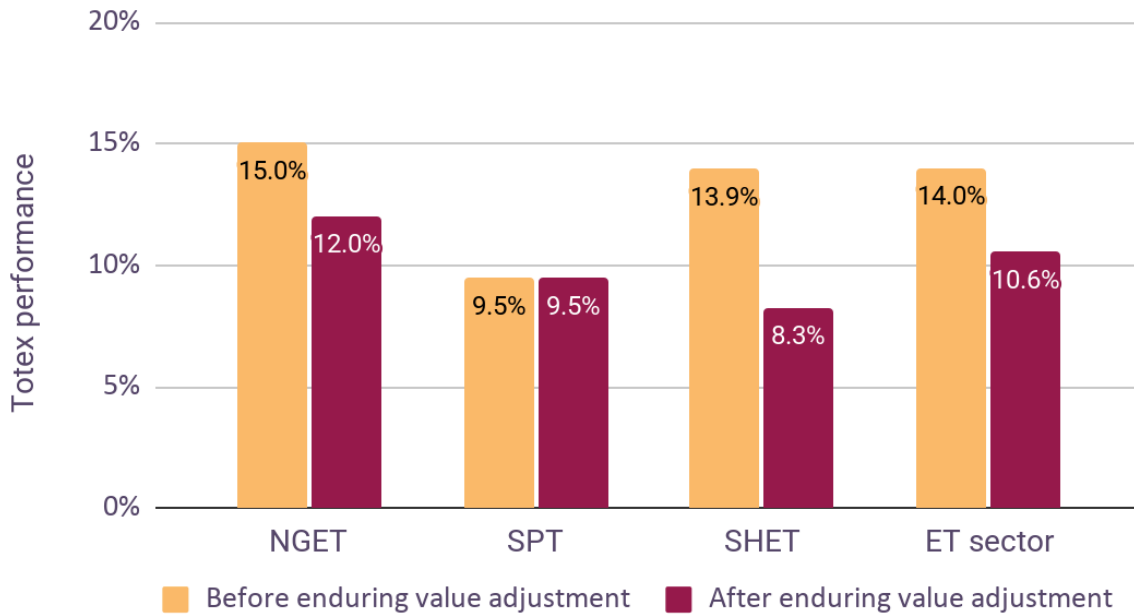
This section examines the performance of electricity transmission companies after the first four years of RIIO-ET2. It examines the areas of total expenditure (totex), output performance and returns.

### a) Totex outperformance

A key element of the RIIO price control is a financial incentive for companies to find cost savings and underspend their total expenditure (totex) allowance. The design of the incentive includes a sharing factor where companies share around half of any underspend with customers. Similarly, any overspend is also shared between companies and customers.

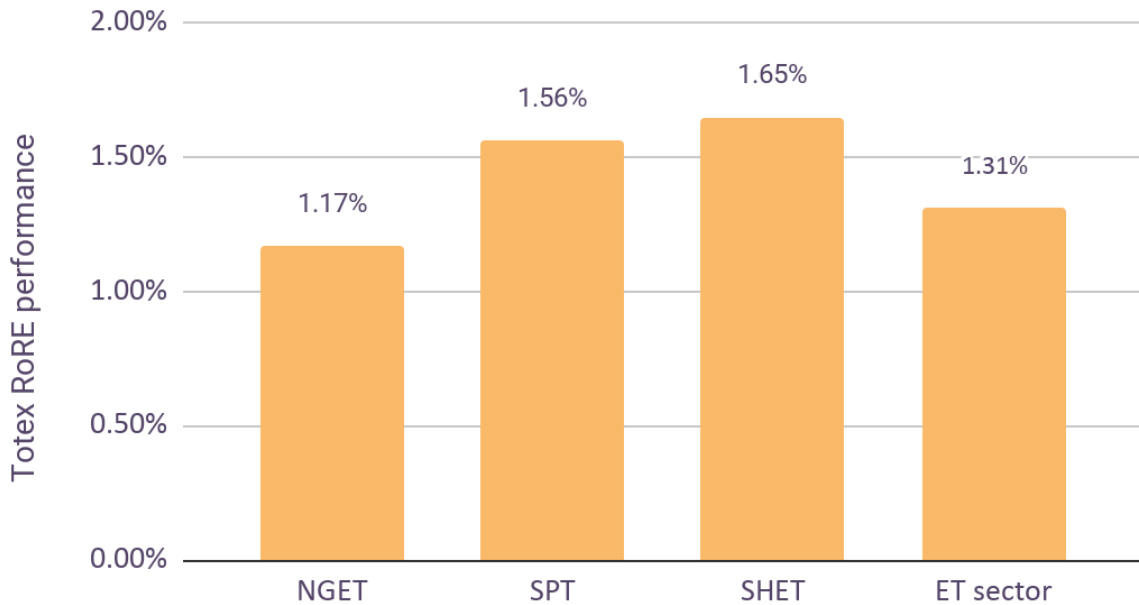
Figure 13 illustrates the totex performance for the first four years of RIIO-ET2, both before and after enduring value adjustments. It shows totex under/overspend for each company as a percentage of annual totex allowance. The chart shows underspend below allowance as a positive figure and overspend as a negative figure. Across ET, all 4 companies are currently underspending their totex allowance.

### **Figure 13: Totex out(under) performance (allowance vs actual/forecast spend) - Cumulative to 2025**



The electricity transmission sector underspent allowances by 14.0% before enduring value adjustments were applied, and 10.6% after enduring value adjustments were applied. When a company underspends (or overspends) against allowances, the difference between the allowance and actual costs is shared between the companies and consumers. This means that, when a company underspends (overspends) against allowances, consumers pay more (less) than the actual costs which leads to increased (reduced) shareholder returns, which are shown as a percentage below (including enduring value adjustments, as published by Ofgem).

**Figure 14: Electricity transmission totex incentive performance by company (% RoRE)**

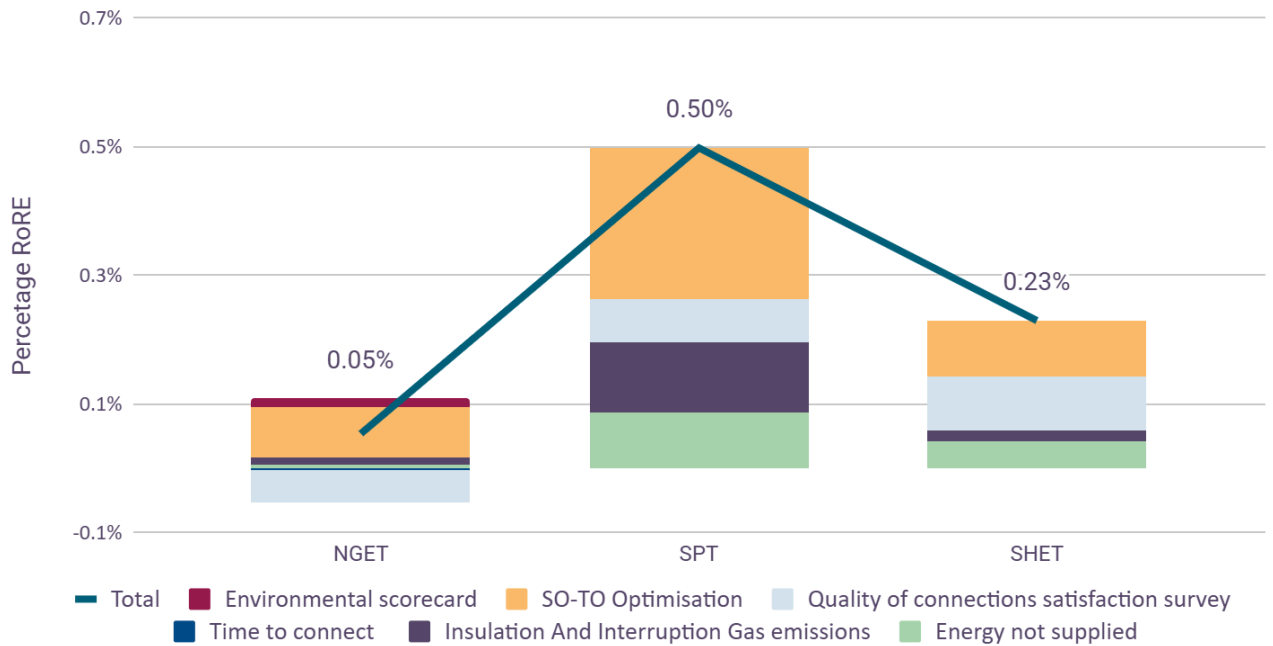


Any under or over spend on totex allowances impacts returns through the totex incentive mechanism. All electricity transmission companies increased returns. Totex incentive RoRE performance is 1.3% across the sector, with the highest performance achieved by SHET at 1.65%.

### **b) Transmission sector output performance**

The RIIO-ET2 price control put in place a range of outputs and incentives including Licence Obligations, Price Control Deliverables (PCDs) and Output Delivery Incentives (ODIs) to drive improved performance. Of the ODI's, these are divided into reputational incentives (ODI-R) and financial (ODI-F) incentives. The common ODI-F incentives, which impacts returns, are shown below.

**Figure 15: RIIO-2 Electricity Transmission output incentive performance**



The aggregate incentive reward ranges from 0.05% RoRE for NGET, who underperformed on its connection survey, to 0.5% for SPT. The main reward for all the companies has been derived from the SO:TO incentive. This was trialled for two years and was then extended to the end of RIIO-ET2. Whilst supportive of an incentive to help the system operator to manage constraint costs, we have previously flagged our concerns that the SO:TO incentive does not represent good value for money<sup>38</sup>. For example, in year 2, the TOs were able to earn over £8 million in incentive rewards compared to costs of £1 million<sup>39</sup>. We believe the same benefits could be achieved for lower costs. Ofgem has changed the scheme for RIIO-3. We are unable to assess at this stage whether this will resolve the issues.

### c) Electricity transmission return on regulated equity (RoRE)

We showed last year that despite Ofgem aiming to tighten returns in RIIO-2, RoRE performance remained at similar levels to RIIO-1. By 2025, outperformance

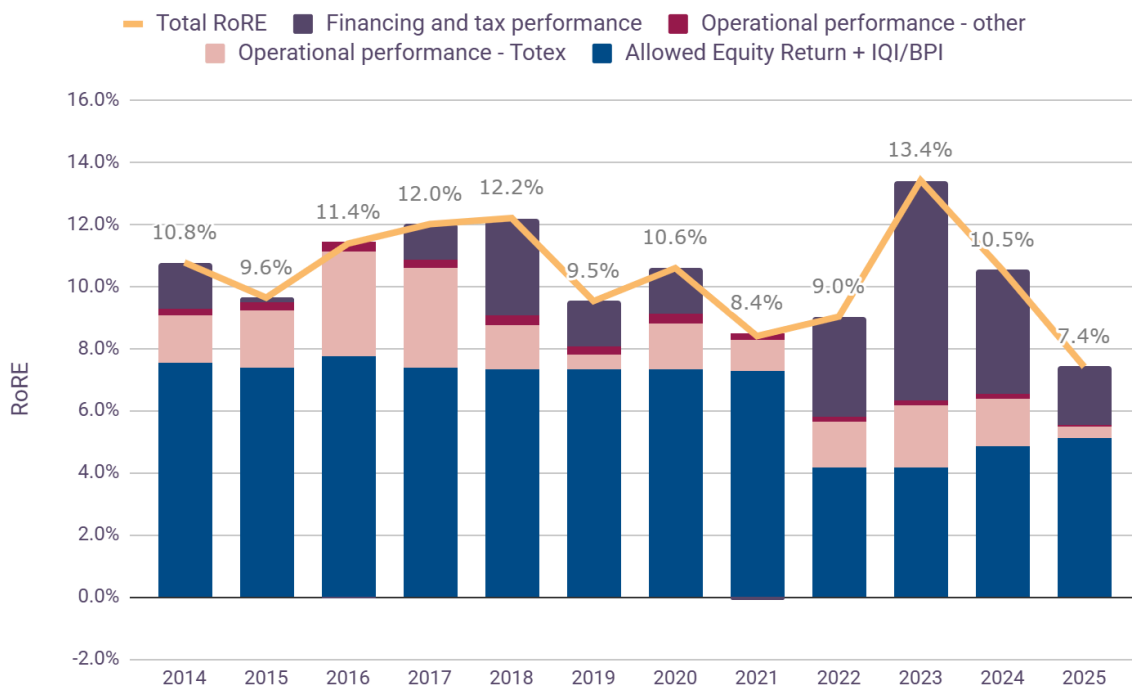
<sup>38</sup> Citizens Advice, [RIIO-3 Sector Specific Methodology for the Gas Distribution, Gas Transmission and Electricity Transmission Sectors](#), March 24

<sup>39</sup> Table 1 [RIIO-2 System Operator: Transmission Owner Optimisation output delivery incentive](#)

has come down only very slightly, and remains at similar levels to RIIO-1. Average sector RoRE performance was 10.6% in RIIO-1, and is 10.1% up to 2025 in RIIO-2. The key changes from RIIO-1 are:

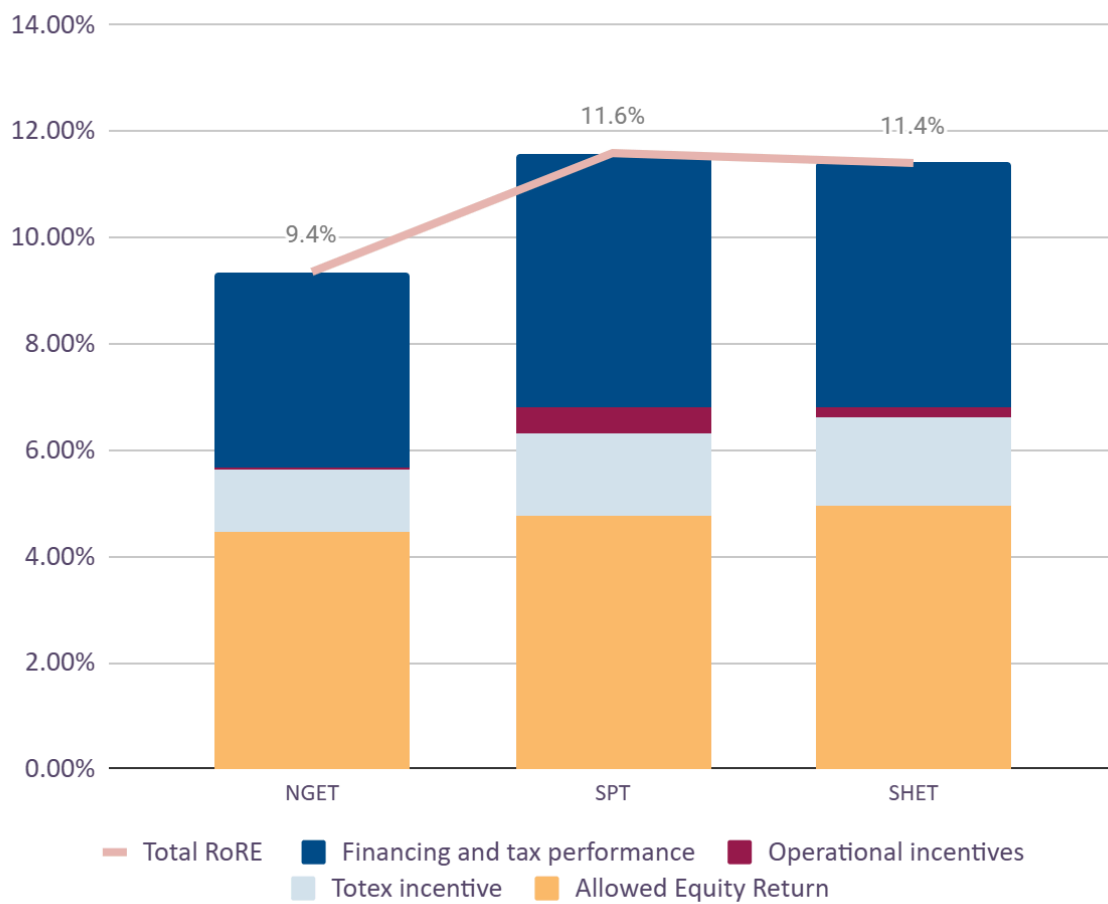
- Totex and output incentives are both lower than RIIO-ET1.
- Financing and tax performance is higher. The average financing/tax benefit during RIIO-ET2 up to 2025 is 4% of RoRE. This equates to a benefit to electricity transmission companies of around £1.9 billion (in £2024/25 prices).

**Figure 16: Electricity transmission sector RoRE performance RIIO-1 (2014 - 2021) versus RIIO-2 to (2022 - 2025)**



Below shows electricity transmission companies' individual performance in RIIO-2 to 2025.

**Figure 17: Electricity transmission company RoRE performance RIIO-2 to 2025**



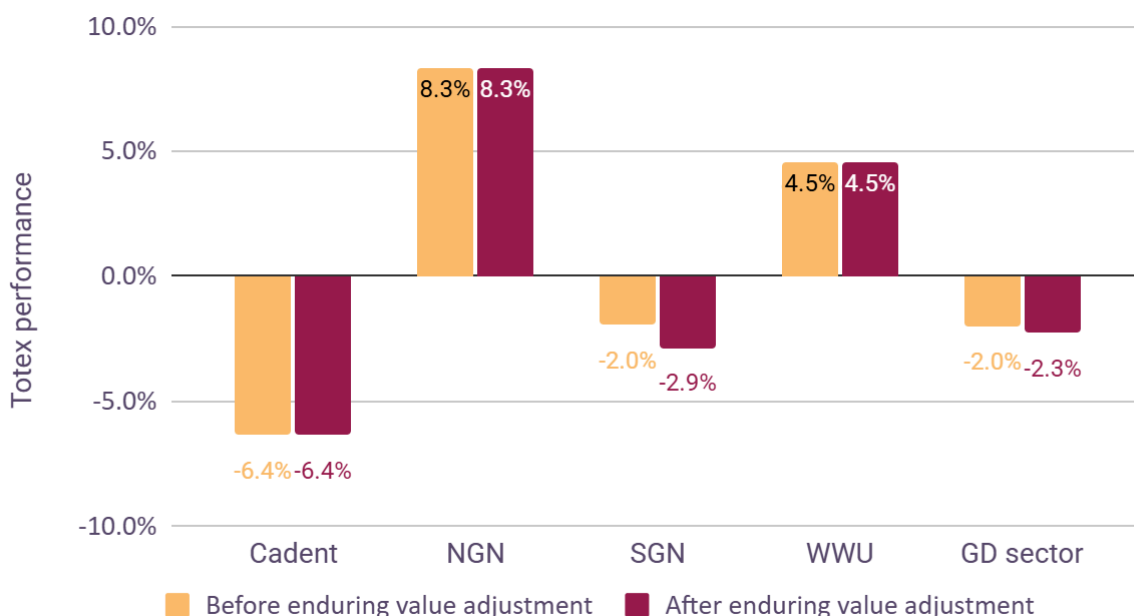
RIIO-2 RoRE performance to 2025 for electricity transmission ranges from 9.4% for NGET to 11.6% for SPT.

# Gas Distribution

## a) Gas Distribution Totex performance

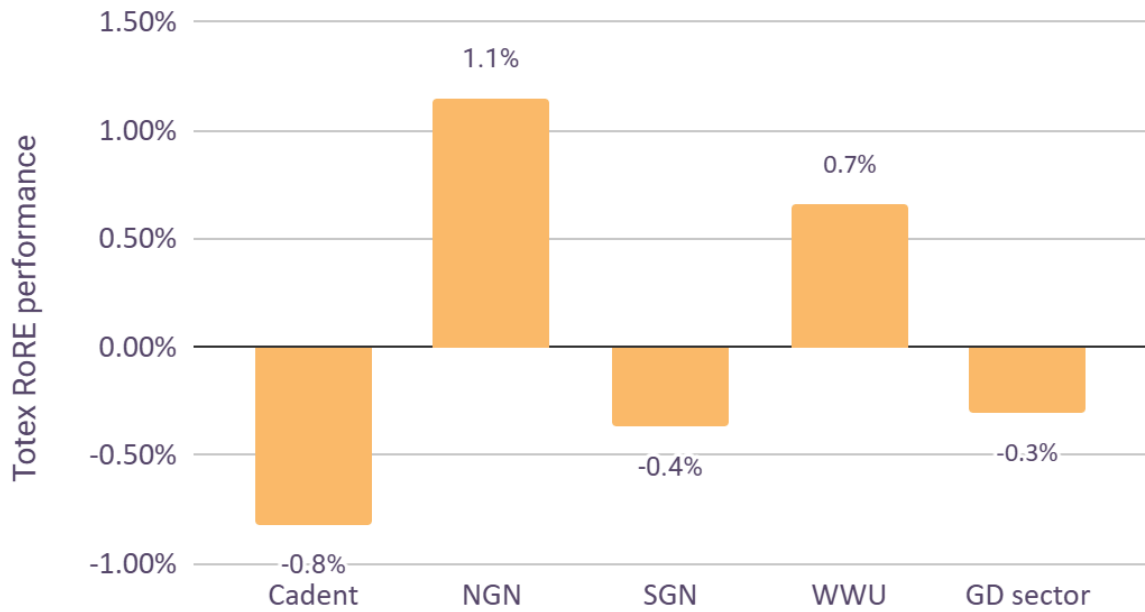
The chart below shows totex performance over the first four years of GD2. It shows totex under/overspend for each company as a percentage of annual totex allowance. The chart shows underspend against allowances as a positive figure and overspend as a negative figure.

**Figure 18: Totex out(under) performance (allowance vs actual/forecast spend) - Cumulative to 2025**



Across the sector, there has been a small net overspend of 2% before enduring value adjustments are applied, and 2.3% after. However, this reflects wide variation across companies. NGN and WWU have underspent, whilst Cadent and SGN have overspent. When a company underspends (or overspends) against allowances, the difference between the allowance and actual costs is shared between the companies and consumers. This means that, when a company underspends (overspends) against allowances, consumers pay more (less) than the actual costs which leads to increased (reduced) shareholder returns, which are shown as a percentage below (including enduring value adjustments, as published by Ofgem).

**Figure 19: totex incentive performance by company (% RoRE)**

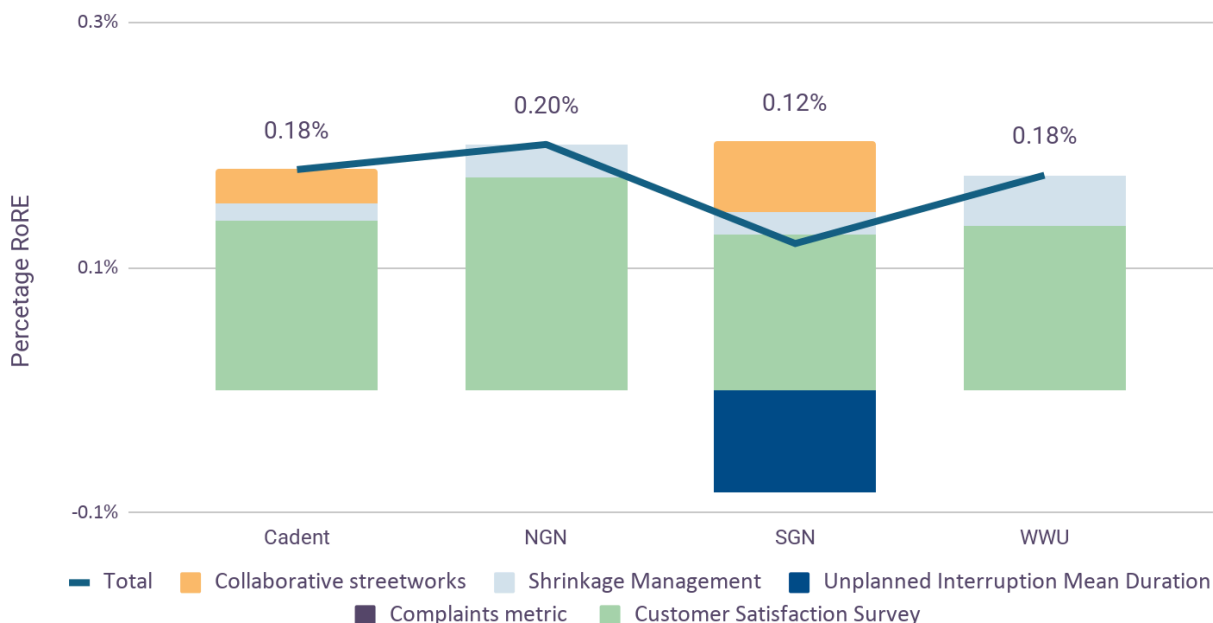


Across gas distribution, the sector has slightly underperformed with totex RoRE performance of -0.3%. Performance across the companies ranges from 1.1% by NGN to -0.8% by Cadent.

### **b) Gas Distribution Output performance**

The main Output Delivery Incentives (ODI) with financial impacts are listed below.

**Figure 20: Gas distribution sector output performance**



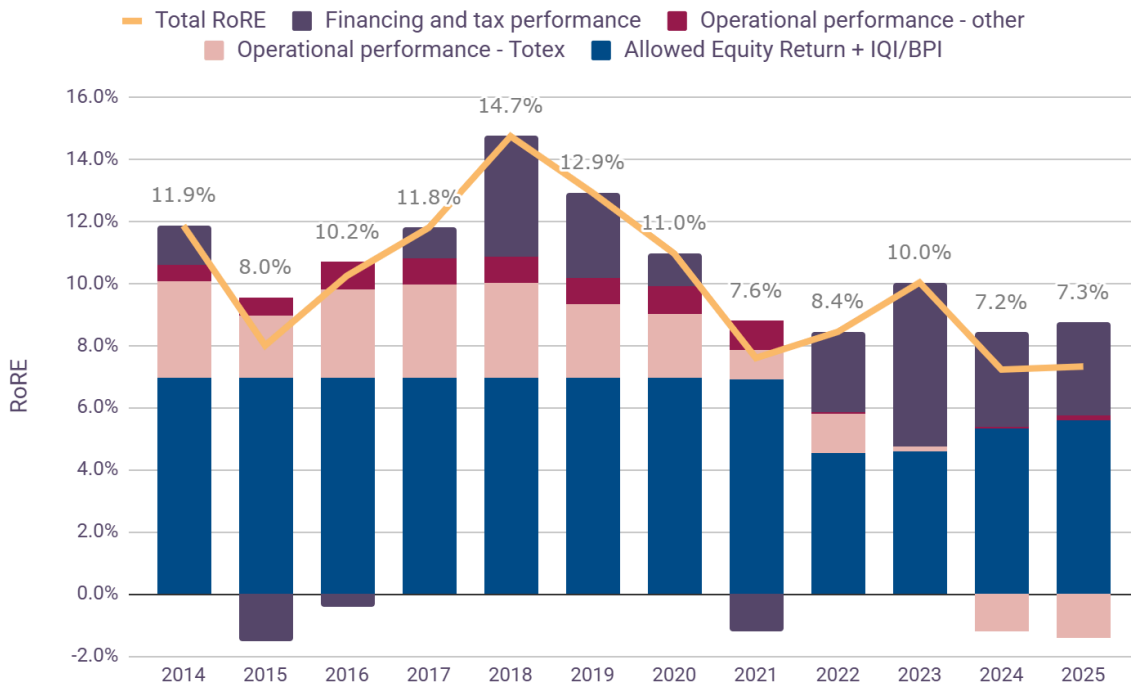
Across the gas distribution companies, all companies have achieved net outperformance across the ODI-Fs. SGN was the only company to underperform on an element, which was unplanned interruptions. The aggregate rewards across companies range from 0.12% by SGN, to 0.20% by NGN.

### c) Gas Distribution RoRE performance

The gas sector distribution RIIO-2 RoRE to 2025 is 8.2%. This compares to an average of 11% for the sector in RIIO-1. The key changes from RIIO-1 are:

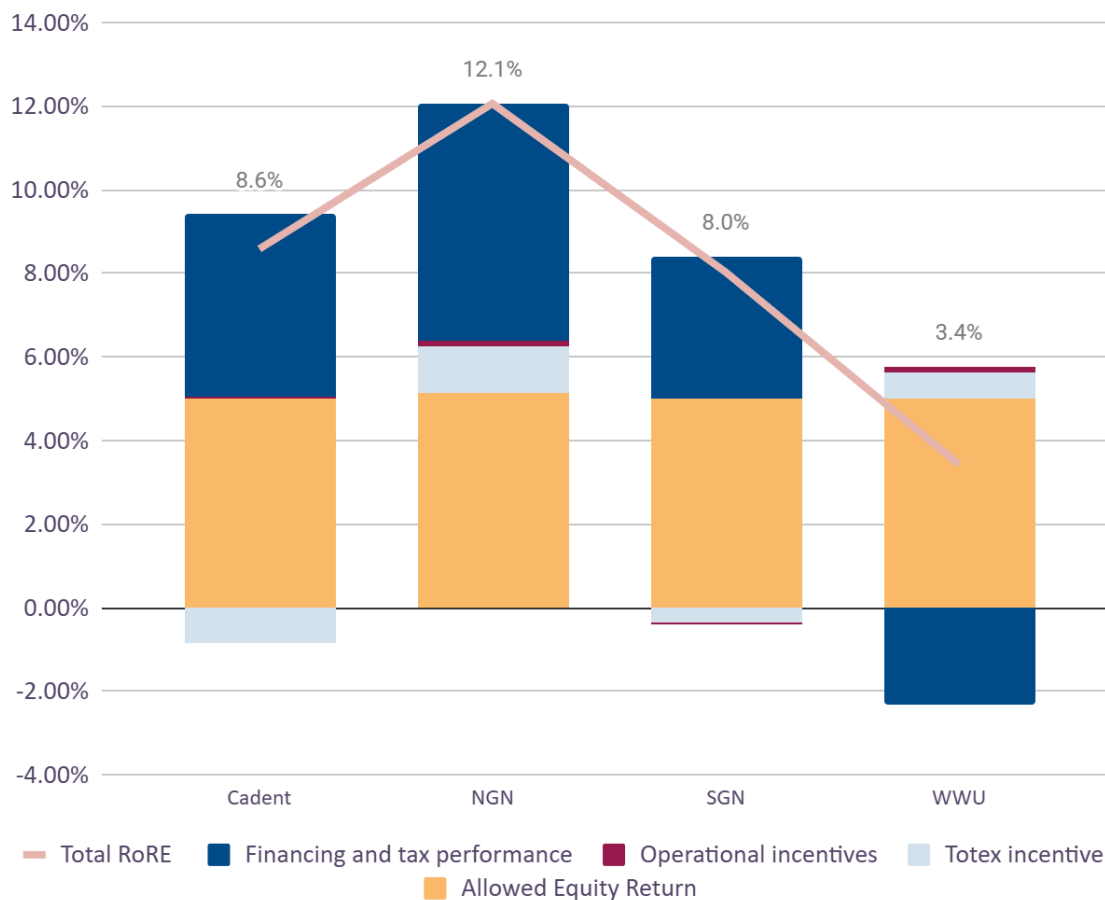
- Totex and output incentives are both lower than RIIO-GD1.
- Financing and tax performance is higher. The average financing/tax benefit during RIIO-GD2 up to 2025 is 3.5% of RoRE. This equates to a benefit to gas distribution companies of around £1.4 billion (in £2024/25 prices).

**Figure 21: Gas distribution sector RoRE performance - RIIO-1 (2014 - 2021) and RIIO-2 to (2022 - 2025)**



Individual RoRE performance for gas distribution companies is shown below.

**Figure 22: Gas distribution RoRE performance RIIO-2 to 2025**



RIIO-2 RoRE performance to 2025 for the gas distribution companies ranges from 3.4% for WWU to 12.1% for NGN. WWU is the only company across all sectors to underperform relative to the baseline allowed cost of equity.

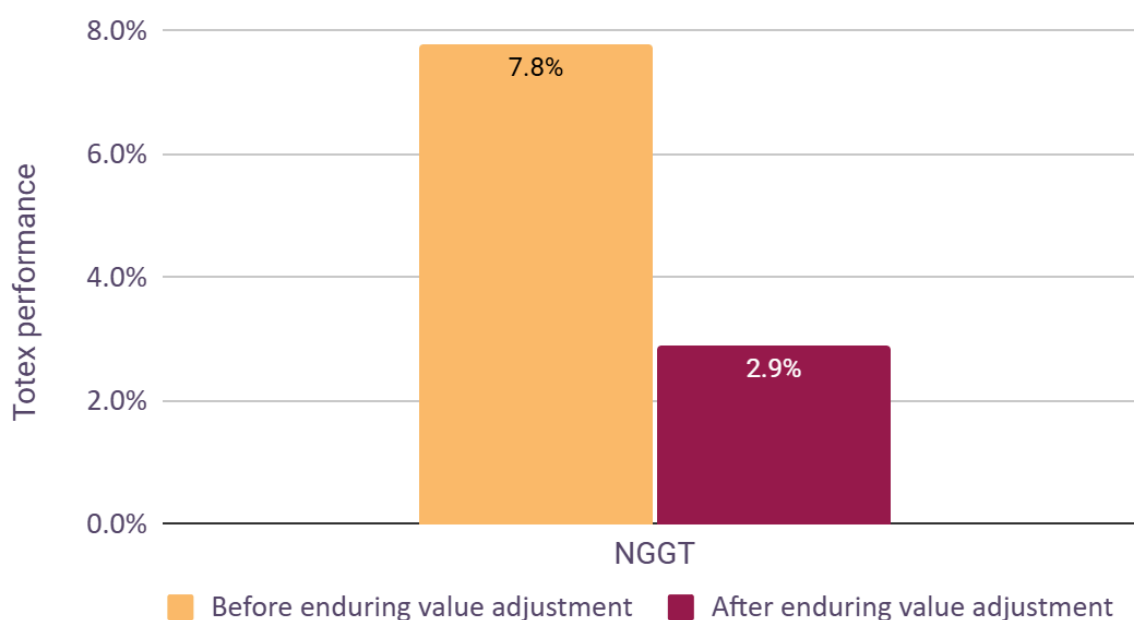
## Gas Transmission

This section reviews the performance of the National Gas transmission network. It does not include their separate gas transmission system operation business.

### a) Gas Transmission Totex

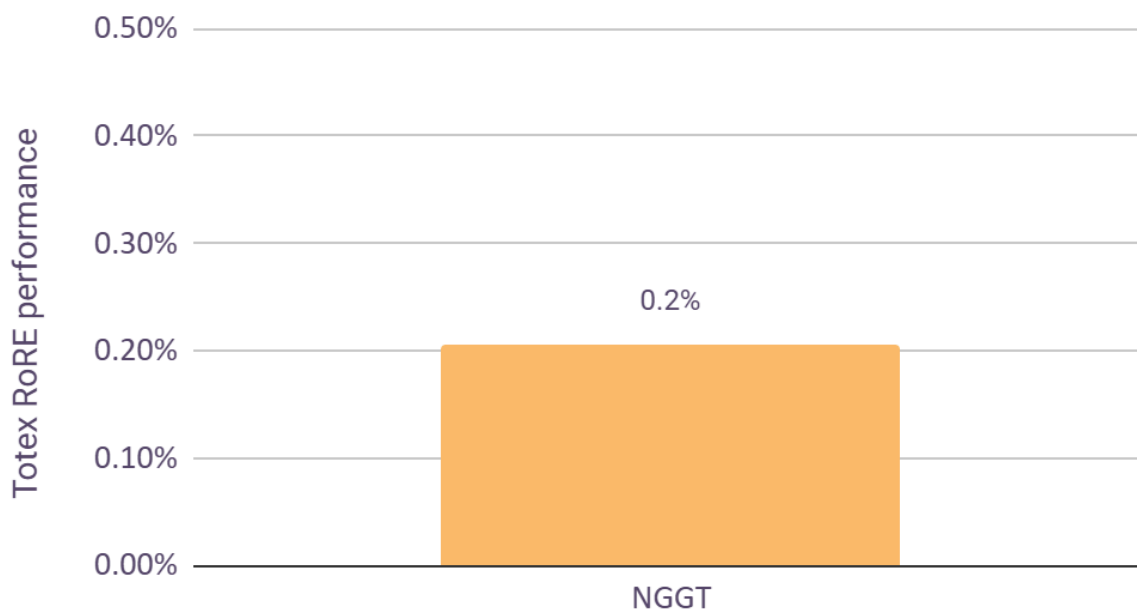
The below shows that National Gas has underspent its allowances by 7% up to 2025.

**Figure 23: Gas transmission totex out(under) performance (allowance vs actual/forecast spend) - Cumulative to 2025**



NGGT has underspent by 7.8% before enduring value adjustments are applied, and by 2.9% after. When a company underspends (or overspends) against allowances, the difference between the allowance and actual costs is shared between the companies and consumers. This means that, when a company underspends (overspends) against allowances, consumers pay more (less) than the actual costs which leads to increased (reduced) shareholder returns, which are shown as a percentage below (including enduring value adjustments, as published by Ofgem).

**Figure 24: Gas Transmission totex incentive performance by company (% RoRE)**



National Gas demonstrated totex RoRE performance of 0.21%.

**b) Gas Transmission output performance**

The key financial output delivery incentives for Gas Transmission are:

- **Customer satisfaction survey:** improve quality of customer service
- **Environmental scorecard:** rewarding achievement of several environmental outcomes

The cumulative output performance over the first four years of the RIIO-2 period for the key financial Output Delivery Incentives is shown below for National Gas.

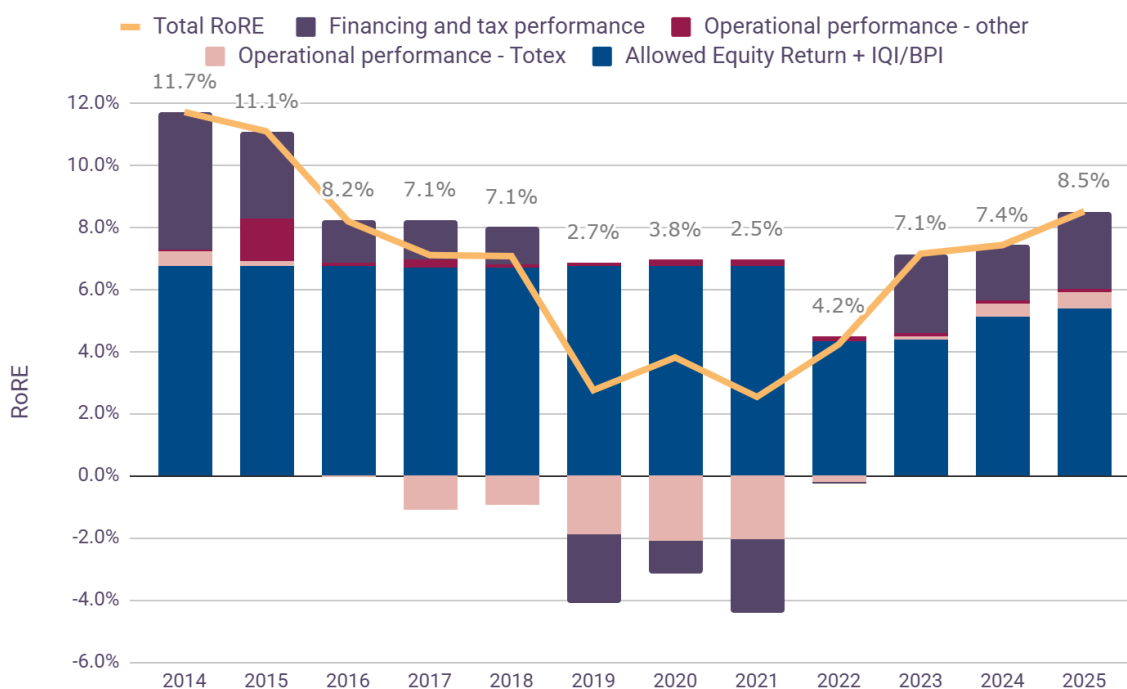
**Figure 25: Gas Transmission Output performance**

Output incentives	RoRE (%)
Customer satisfaction survey	0.16%
Environmental scorecard	0.00%

### c) Gas Transmission RoRE

Whilst Ofgem sought to reduce returns in RIIO-2, there has been no change between average RIIO-1 returns and RIIO-2 returns to 2025. Both sit at 6.8%.

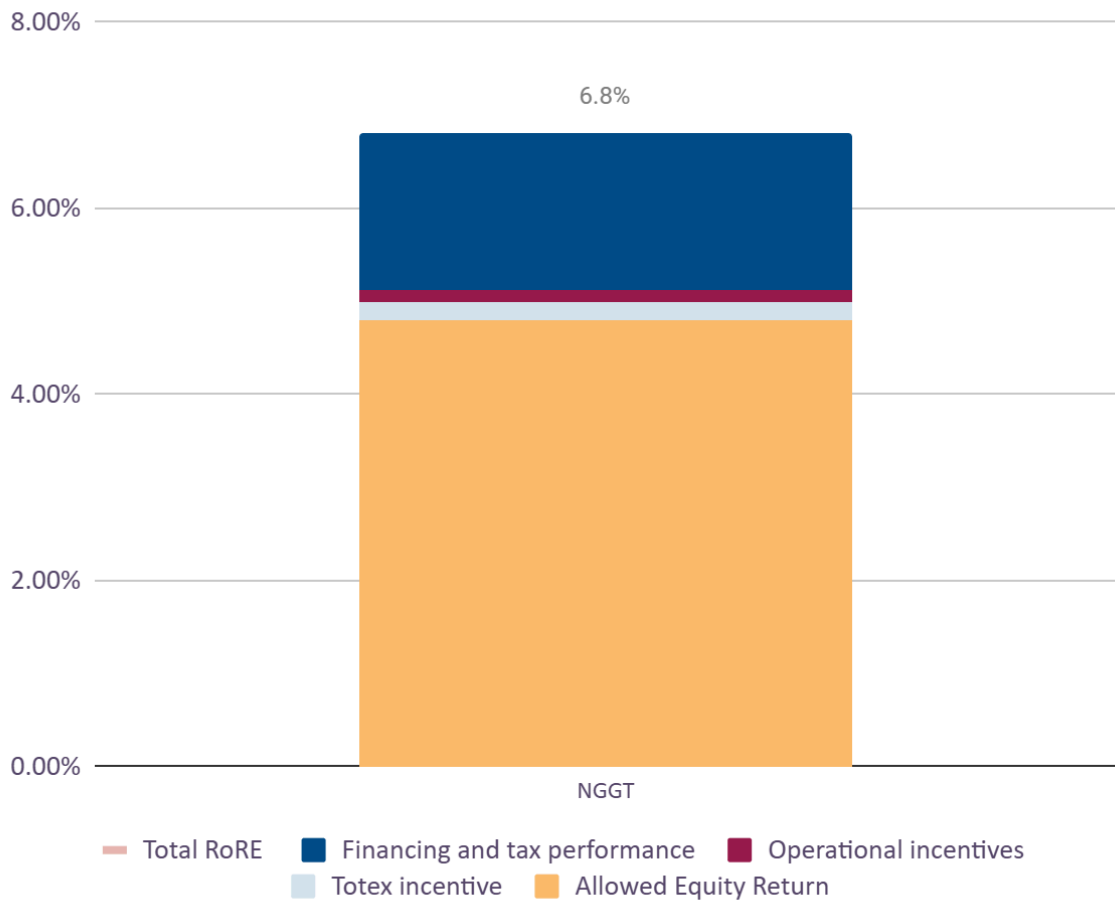
**Figure 26: Gas transmission sector RoRE performance - RIIO-1 (2014 - 2021) and RIIO-2 to (2022 - 2025)**



Below shows average RIIO-2 RoRE to 2025. The key changes from RIIO-1 are:

- Totex performance has increased.
- Other operational performance has decreased.
- Financing and tax performance has increased to 1.7%. This has brought about investor benefits of £196 million.

**Figure 27: Gas transmission RoRE performance RIIO-2 to 2025**



The financing/tax benefit during RIIO-GT2 up to 2025 equates to a benefit to national gas of around £196 million (in £2024/25 prices).

## Electricity Distribution

The electricity distribution price control covers the five-year period between 1<sup>st</sup> April 2023 and 31<sup>st</sup> March 2028. Ofgem's objectives for RIIO-ED2 were:

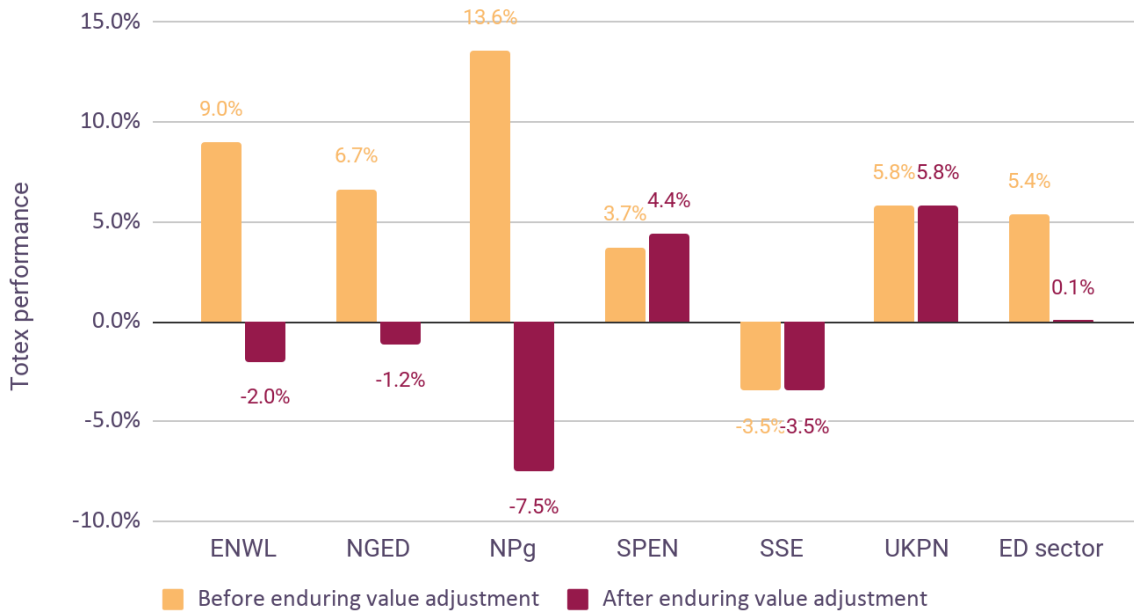
- delivering the local energy distribution networks needed for net zero, enabling the connection of electric vehicles and heat pumps
- supporting a smarter, more flexible, and digitally enabled energy system, which should improve network efficiency
- ensuring network reliability by reducing the frequency and duration of power cuts
- delivering high quality services to customers and network users
- ensuring no one is left behind in the energy transition
- delivering at lowest cost to consumers.

This section examines the performance of electricity distribution companies after the first two years (2024/25) of RIIO-ED2. It examines the areas of total expenditure (totex), output performance and returns.

### a) Electricity Distribution totex

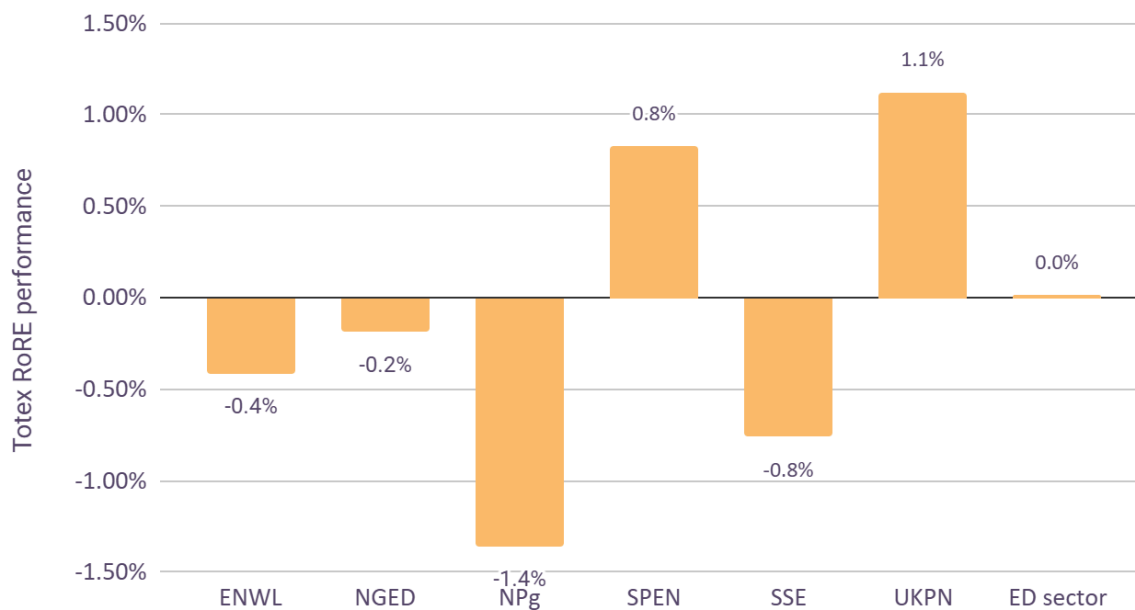
The following chart (Figure 30) illustrates the totex performance for 2024/25, the first two years of RIIO-ED2. The chart shows underspend below allowance as a positive figure and overspend as a negative figure.

### Figure 28: Totex out(under) performance (allowance vs actual/forecast spend) - Cumulative to 2025



Across the sector, there has been an underspend of 5.4% before enduring value adjustments are applied, falling to a 0.1% underspend after enduring value adjustments are applied. This reflects varying performance across the sector. Before enduring value adjustments are applied 5 DNOs underspent and 1 overspent, after enduring value adjustments are applied 2 underspent and 4 overspent. When a company underspends (or overspends) against allowances, the difference between the allowance and actual costs is shared between the companies and consumers. This means that, when a company underspends (overspends) against allowances, consumers pay more (less) than the actual costs which leads to increased (reduced) shareholder returns, which are shown as a percentage below (including enduring value adjustments, as published by Ofgem).

**Figure 29: totex incentive performance by company (% RoRE)**



UKPN achieved the highest totex RoRE performance of 1.1%, whilst NPg received the largest underperformance of -1.4%. Performance across the sector balanced out to 0%.

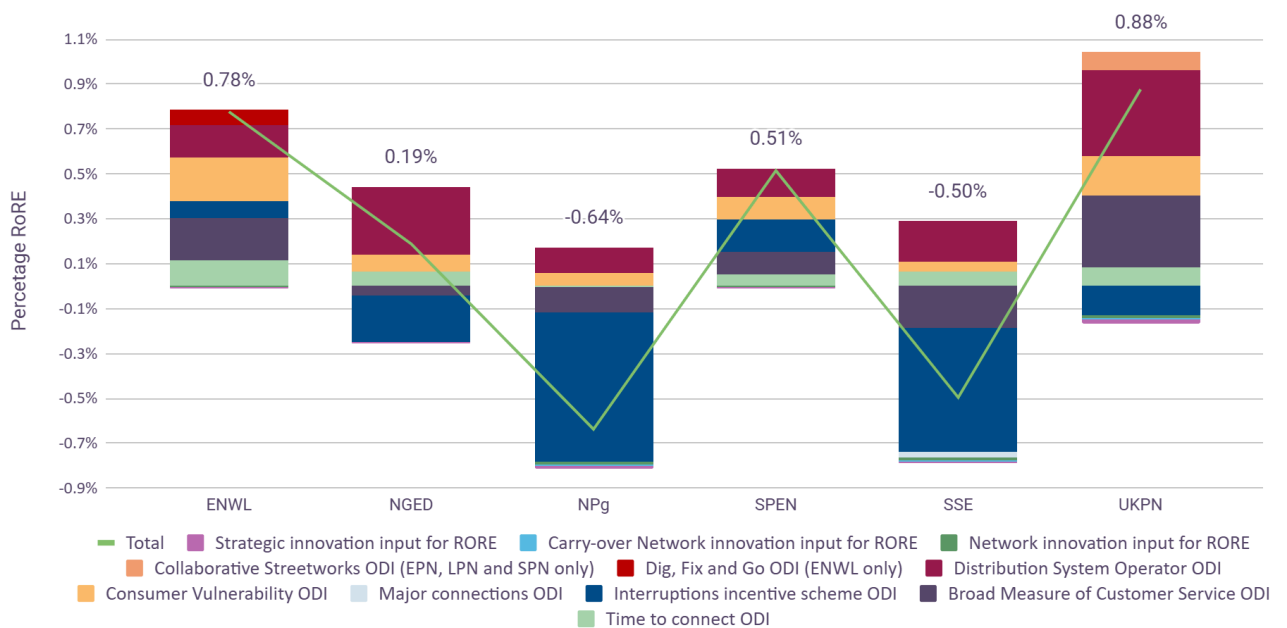
## **b) Electricity Distribution Output performance**

The common ODI-Fs for electricity distribution are:

- **Interruptions Incentive Scheme:** to improve network reliability and reduce the number of interruptions and their length
- **Customer service Incentive:** to improve quality of customer service
- **Consumer Vulnerability Incentive:** to provide appropriate support services for customers in vulnerable situations
- **Major Connections Incentive:** to improve quality of service for major connection customers
- **Time to Connect Incentive:** to reduce time to connect for smaller customers such as domestic connections
- **Distribution System Operator (DSO) Incentive:** to incentivise more efficient network development and operation, considering smart and flexible alternatives to network reinforcement.

Below shows RoRE performance against these metrics:

**Figure 30: Electricity distribution sector output performance**



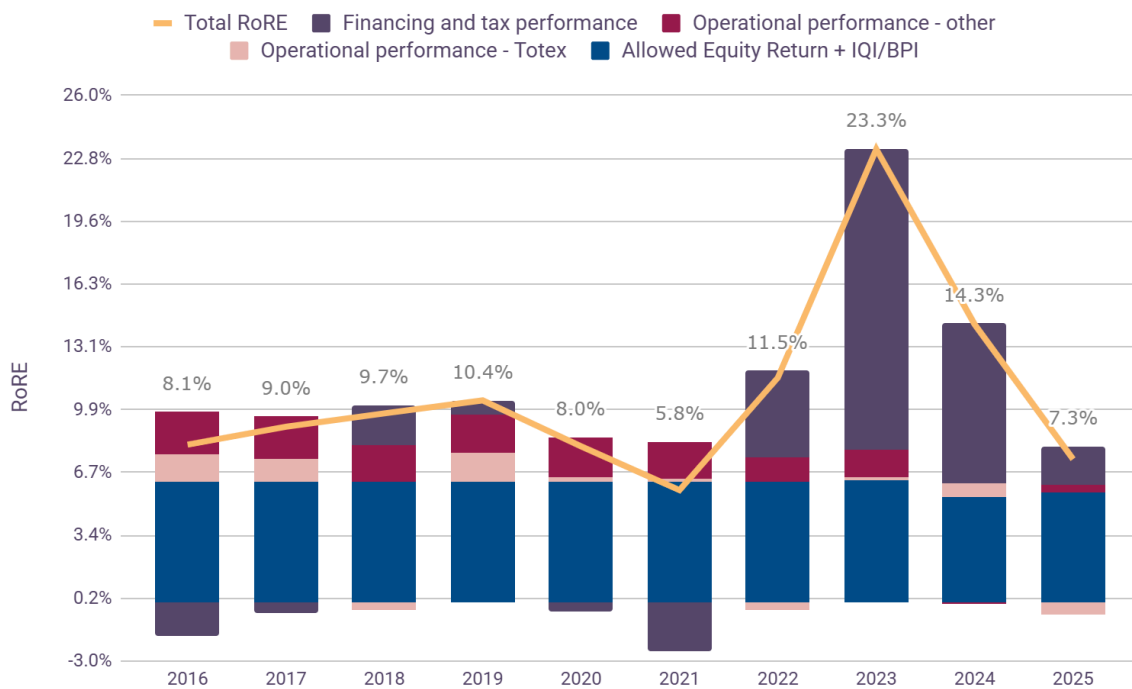
Output performance ranged from -0.64% for NPg to 0.88% for UKPN. ENWL was the only company who did not underperform any output incentive.

### c) Electricity distribution RoRE

As shown in the chart below, unlike the other sectors, the cost of living crisis spans both RIIO-1 and RIIO-2 for electricity distribution. Despite Ofgem trying to tighten returns between ED1 and ED2, they have stayed broadly the same. Average RoRE performance in ED1 was 10.7%, and this has risen slightly to 10.8% in ED2 to 2025. The key changes from RIIO-1 are:

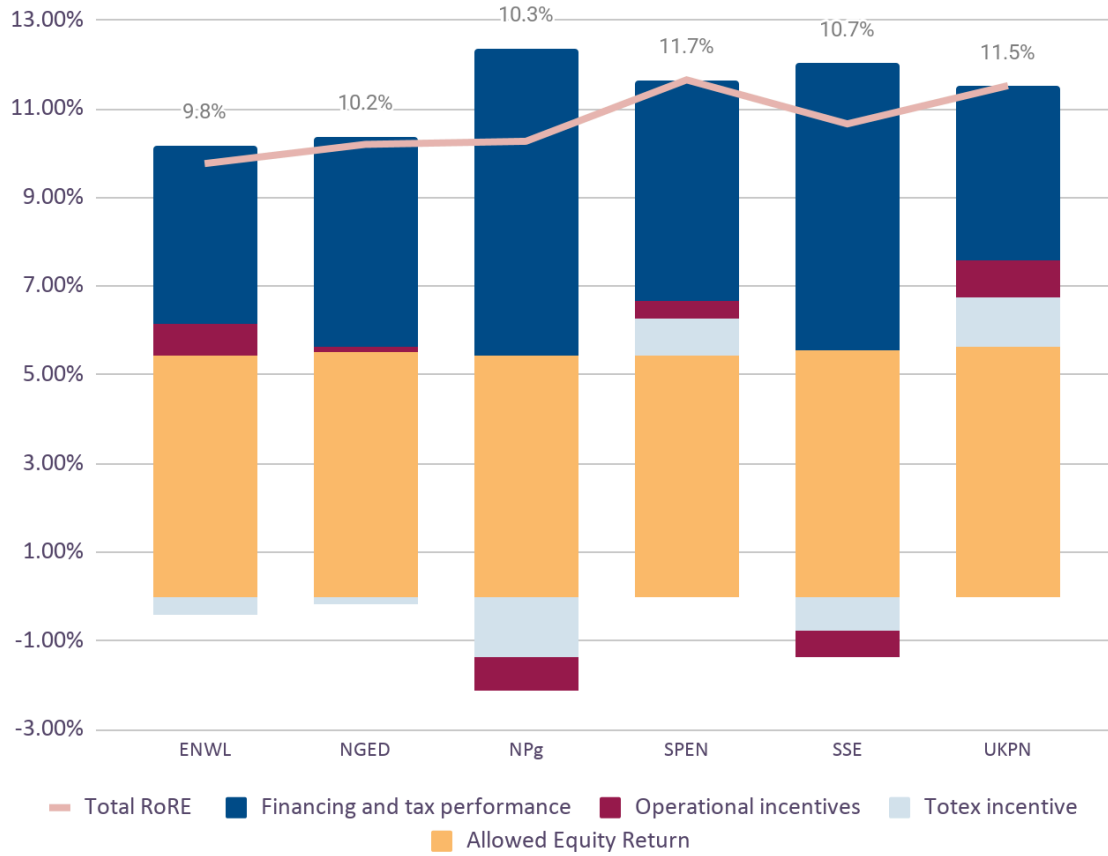
- Totex and output incentives are both lower than RIIO-ED1.
- Financing and tax performance is higher. The average financing/tax benefit during RIIO-ED2 up to 2025 is 5.1% of RoRE. This equates to a benefit to electricity distribution companies of around £1.5 billion (in £2024/25 prices).

**Figure 31: Electricity distribution sector RoRE performance - RIIO-1 (2016 - 2023) and RIIO-2 to (2024-2025)**



The chart below shows individual RoRE performance for the companies.

**Figure: Electricity distribution sector RoRE performance RIIO-2 to 2025**



RoRE performance across the DNOs ranges from 9.8% for ENWL to 11.7% for SPEN.

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