Overview of the UK Renewable Subsidy Schemes

Over the past two decades, the UK has become one of the world's leaders in renewable energy. Wind, solar, and other low-carbon technologies now supply a large share of the country's electricity, reaching a new record level of 69.8% in Q2 2025*. This transition was made possible through carefully designed government support schemes that encouraged investment. Specifically, renewables in the UK have been brought to market by three main subsidy schemes: Renewables Obligation (RO), Feed-in Tariffs (FiT), and Contracts for Difference (CfD). Each scheme was introduced at a different stage of the industry's development, but they all shared the same goal: to attract long-term private capital into projects that would ultimately deliver cleaner, cheaper, and more secure energy for the UK.

Now, as the government consults on changes to how inflation indexation works for the older schemes (RO and FiT), it's important to understand how these subsidies actually work and what is at stake if the rules are changed.

Earlier models: RO and FiT

The Renewables Obligation (RO) was introduced in 2002 to encourage large-scale renewable electricity generation. Under this system, renewable energy generators received "Renewables Obligation Certificates" (ROCs) for every unit of electricity they produced. Electricity suppliers were then required to buy these certificates, providing generators with an additional income stream on top of the wholesale electricity price. The typical length of Renewables Obligation support is 20 years.

The Feed-in Tariff (FiT), which was introduced in 2010, was aimed at smaller-scale generators such as rooftop solar. It guaranteed a fixed price for every unit of electricity produced, again giving investors certainty over future income. FiT support tends to last for 20-25 years.

Both the RO and FiT schemes are now closed to new projects (RO closed in 2017 and FiT closed in 2019), but existing assets continue to receive payments under the original terms. These payments are currently adjusted for inflation annually in line with the Retail Prices Index (RPI).

Existing model: CfD

The Contracts for Difference (CfD) scheme, introduced in 2014, replaced earlier subsidy models and reflects how renewable energy has become more affordable in recent years. Under the CfD system, renewable generators take part in a competitive auction and bid the price per unit of electricity needed to make projects viable, which is known as the strike price. Generators who win the auction are guaranteed this strike price. When the wholesale electricity price is below the strike price, the government tops up the difference ensuring the generator continues to receive the agreed amount. Conversely, when the market price is higher than the strike price, the generator pays back the difference. In this way, CfD acts as a natural hedge for consumers.

When wholesale electricity prices rise, the subsidies funded by consumers fall as less support is needed to bridge the gap between the market price and the strike price. In extreme cases, when prices are exceptionally high, generators may be required to pay money back into the scheme, creating a surplus in the subsidy pot. This is very different from the earlier schemes, where payments were fixed regardless of market conditions.

It is worth noting that strike prices have fallen considerably over time, apart from a modest rise from 2022-24 linked to global supply chain pressures. CfDs are continuing to provide better value to billpayers year on year. For instance, contracts awarded for offshore wind generators in Auction Round 4 at £52.04 per MWh (2024 real terms), are 68% lower than CfDs awarded in Auction Round 1 at £165.13 per MWh (2024 real terms).

Table 1 – Summary of key differences between the three main renewable subsidy schemes

	RO	FiT	CfD
Effective period	2002-2017	2010-2019	2014-present
How price was set	Based on market trading with a regulated buyout floor price	Fixed administratively based on tech cost and desired return	Set through competitive auction bids
Who set it	Government + Market	Government	Market (via auction)
Indexation	RPI	RPI	CPI

Government consultation on moving RO and FiT from RPI to CPI

Historically, RPI has reflected a higher rate of inflation compared to other indices such as the Consumer Prices Index (CPI). This is largely due to differences in calculation methodology, with RPI including housing costs such as mortgage interest payments and private rents. As a result, the methodology for calculating RPI is scheduled to be phased out by 2030 and replaced with new methodology. The Office for National Statistics (ONS) has also noted that RPI is a less suitable measure of inflation for renewable subsidy schemes, given that housing costs are largely unrelated to the underlying cost drivers in the energy sector.

Further to this, the UK government recently cited the view that indexing to RPI has historically overcompensated generators, contributing to higher policy costs and therefore announced plans to change the indexation for RO and FiT schemes from RPI to CPI, proposing two potential options:

- Option 1: an immediate switch to CPI Indexation from April 2026 onwards;
- Option 2: a temporary freeze of prices at the 2025/26 level, with no inflation-linked increase applied until the cumulative effect of CPI-based inflation aligns with the current RPI-adjusted price. This is effectively to apply CPI indexation retrospectively.

While we recognise the rationale for moving away from RPI, we do not consider either of the proposed options to be appropriate. Changing indexation mid-way through the support period risks distorting project valuations and market signals, while offering limited practical benefit given that overall scheme costs are already naturally declining. Per DESNZ's own estimates, the projected savings amount to as little as £3 - £5 for per annum, per household**.

Starting around 2027, the total amount paid under these schemes will begin to fall sharply as older projects reach the end of their support periods. Over the following decade, these payments will tail off to zero (the final RO contracts expire in 2037). As such, the associated cost to consumers will naturally unwind without the need for further government intervention. An alternative option would be to reduce the level of RO and FiT subsidies today but extend their expiry dates to deliver the same overall value.

This approach would preserve investor protections by maintaining the total support they receive, while also easing the current cost burden on consumers through lower near-term subsidy payments.

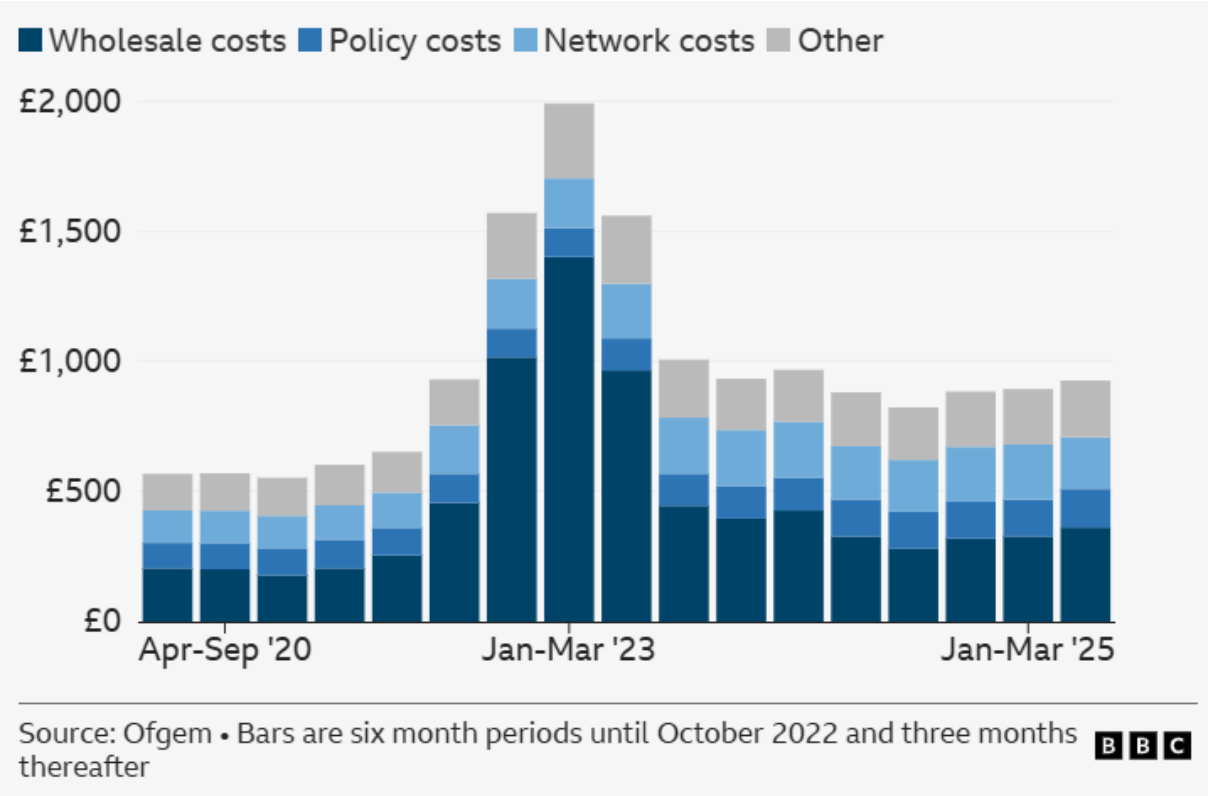
Understanding energy bills and where costs come from

It's also important to look at the bigger picture. Energy bills comprise multiple components, so understanding the key cost drivers is essential to properly assess the government's proposal.

Table 2 – Electricity bill breakdown

	What is it?	Approx. %
Wholesale costs	This is what energy suppliers pay to purchase electricity from the generators before selling it to households or businesses. The UK operates under a "marginal pricing" system, meaning that the wholesale cost is set by the last (and typically most expensive) generator required to meet overall demand – often gas.	35 – 50%
Network costs	This is the transmission and distribution cost of getting power from generators to homes and businesses.	20 – 25%
Environmental and social obligation costs "green levies"	These typically include subsidies and levies that support renewable energy and social schemes which are passed through to consumers.	15 – 20%
Other costs	These include supplier operating costs and margins, VAT and other taxes, etc.	15 – 20%

Chart 1 – Electricity bill components breakdown



Gas-fired power plants often provide the marginal unit of supply, meaning their costs set the overall wholesale price. Consequently, as shown in the chart above, when gas prices rise (as we saw dramatically after 2021), electricity prices follow even though renewable generation costs remain largely unchanged.

While renewables subsidies are visible in the "green levy" portion of bills, they are not the biggest driver and are already shrinking. The dramatic rise in bills in recent years has instead been primarily caused by elevated gas prices following global supply disruptions. Renewables have actually helped lower bills by displacing expensive gas generation and enhancing the security and resilience of the UK's energy mix.

Why redistribution by stealth is the wrong approach

A significant share of UK renewable assets is owned by UK pension funds, insurance companies, and retail investment vehicles. These investors represent the savings and pensions of ordinary people. If the government were to retroactively change how indexation works under the RO and FiT schemes, it would effectively reduce the value of those long-term investments, undermining confidence in the UK as a stable and predictable market for infrastructure capital. That, in turn, means pension holders and retail investors would bear the cost. It would amount to a redistribution by stealth — taking value from ordinary savers to deliver short-term relief on bills that are already affected far more by gas prices and global markets.

If the goal is to reduce the burden on electricity bills, a fairer and more transparent approach would potentially be to move the funding for legacy renewable subsidies off electricity bills entirely and instead finance them through general taxation or a small levy on gas consumption. This would better reflect the true drivers of energy costs and avoid undermining investor confidence in the UK's long-term infrastructure framework.

Seeing subsidies as an investment, not a cost

Finally, it is vital to remember why these subsidies were introduced in the first place. They were not handouts. Instead, they were investments in building a cleaner, more resilient energy system.

The benefits are long-lasting:

- Lower-cost electricity beyond the original subsidy period, as projects continue to operate after their contracts expire;
- Greater energy security, by reducing reliance on volatile imported gas;
- A greener energy mix, helping the UK meet its net-zero commitments;
- Economic growth, job creation, and technological innovation as the renewables sector grows; and
- Mitigation of climate change, which, while a global challenge, brings real and local economic and environmental benefits.

By supporting renewables early, the UK helped drive down global costs, making clean energy affordable for everyone today. Changing the rules after the fact risks undoing that leadership and damaging the credibility that took decades to build.

Concluding remarks

Renewable energy is a mature technology, meaning the industry can continue to lower costs through ongoing economies of scale and stronger and more efficient supply chains. It is also important to acknowledge that legacy subsidies for the industry (RO and FiT) will begin to decline from 2027 as it reaches full maturity, while the newer CfD model is offering better value to the customer as evidenced by lower strike prices in competitive auctions.

Revisiting indexation now would not meaningfully reduce bills, but it would send a worrying signal to investors and penalise UK savers and pension holders. The smarter path is to recognise renewables support as a strategic investment that continues to pay dividends in cleaner air, energy independence, and lower costs for future generations.

**Source: Energy Trends: September 2025 - GOV.UK*

***Source: https://www.gov.uk/government/consultations/feed-in-tariffs-fit-scheme-indexation-changes/changes-to-inflation-indexation-in-the-feed-in-tariffs-fit-scheme-consultation-document-html.*