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Default Market Offer prices 2025 – 26: Draft Determination

Submission via email: DMO@aer.gov.au

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AGL Response to Default market offer prices 2025 – 26 draft determination

AGL Energy (**AGL**) welcomes the opportunity to comment on the Default Market Offer (DMO) prices 2025 – 26 draft determination (**draft determination**).

We broadly support the AER's draft determination, including the clear and transparent manner in which many of the costs have been analysed. We consider it critical that the DMO is set at a level which allows retailers to earn a reasonable return to remain viable and facilitate continuation of competition that has benefitted consumers. Major cost components, including network costs, continue to increase due to long term structural factors. Retailers cannot mitigate the future risk of network cost increases. Addressing those factors is in our view key to ensuring the costs faced by retailers in the future are appropriately managed, as those costs will be reflected in the DMO.

Attached to this letter is our response to the draft determination. In summary we:

- support the approach for determining representative load profiles
- request further information to understand the apparent suppression of increased contracting costs in the calculation of the WEC.
- disagree with the risky decision to use the 75th percentile of modelled costs rather than a prudent approach incorporating the 95th percentile.
- support the approach to benchmarking retail costs and margin.

We look forward to further engagement with the AER and industry on these challenging issues.

If you have any queries about this submission, please contact Kyle Auret on 0422 165 705 or kauret@agl.com.au.

Yours sincerely,

Ralph Griffiths
General Manager, Policy and Market Regulation



Attachment: AGL response to the 2025-26 DMO draft determination

About AGL

Proudly Australian for more than 185 years, AGL supplies around 4.5 million energy services. AGL operates Australia's largest private electricity generation portfolio within the National Electricity Market (NEM), comprising coal and gas-fired generation, renewable energy sources such as wind, hydro and solar, batteries and other firming technology, and gas production and storage assets. We are building on our history as one of Australia's leading private investors in renewable energy to now lead the business of transitioning to a lower emissions, affordable and smart energy future in line with the goals of our Climate Transition Action Plan.

Purpose of the DMO and the information it provides

The purpose of the DMO is to both establish a regulated safety net by limiting standing offer prices and to set a comparison reference price for consumers for market offers. In undertaking the regulatory process to set the DMO, the AER provides an independent assessment of the cost components of a representative retailer's costs of supply, which include wholesale market, network, environmental and retail and other costs.

In the context of the continued cost of living pressures, this information provides important public transparency on the material cost drivers that are impacting customer bills. A consistent and transparent methodology is essential. In addition to informing the standing offer and reference price for customers, the AER's independent assessment should inform government decision makers of those cost drivers, thus assisting to guide public policy which may reduce the underlying cost components.

We note that the fundamental cost drivers are structural and cannot be addressed or suppressed through the DMO. Sustainable reductions in prices will require sustainable reductions in the cost of supply. Network costs continue to grow quickly, primarily driven by a higher rate of return and inflation. These increases are occurring despite the continued low utilisation rates of the monopoly infrastructure. Recovery of NSW REZ development costs is also increasing the network cost component in NSW. Wholesale costs have moderated since their peak, however sustained investment in new generation, storage and firming is required to transform the system and replace aging generators. Effective integration of customer energy resources and the right long term market design settings continue to be critical.

Retailer costs are also growing due to increased regulatory requirements and other necessary costs to provide this essential service. Many of these costs reflect the heightening service obligations of electricity retailers, particularly in servicing customers in hardship and the treatment of bad and doubtful debt.

We note there has been significant scrutiny of retailer operating costs and margins through this regulatory process, the ongoing ACCC retail electricity inquiry, and numerous other government-initiated enquiries. These independent processes consistently demonstrate the competitive retail market is delivering efficient retailer costs. The AER's 2025-26 DMO draft determination should prompt the same level of scrutiny on the regulatory frameworks that are resulting in continued increases in network costs.

It stands to reason that if the Regulator can take into account cost of living pressures in this regulatory pricing decision, this consideration should also carry through to the regulated return on network infrastructure and network pricing approvals.

Wholesale Energy Costs – Representative Customer Load

The draft determination proposes to continue to include both accumulation meter and interval meter data when constructing the retailer's representative customer load. The alternative option proposed in the 2025-26 DMO issues paper (Issues paper) was to use only interval meter data. We support the AER's continued use of both types of customer of meter data. As noted in our previous submission, it is essential that the



representative customer load broadly reflects a representative retailer. This should be based on what retailers face in the market. The Net System Load Profile (NSLP), or accumulation meter data, still reflects a significant proportion of a retailer's customer load. Without the incorporation of this load profile, the results would not truly reflect a representative retailer's load profile.

We support the draft determination conclusion that anticipated future adjustments to the NSLP data are not expected to result in the same material adjustment as was observed following the second adjustment to the NSLP data sets following the implementation of 5MS. We continue to consider the NSLP data now reflects a reasonable reflection of accumulation meter consumption data.

Further Guidance of the WEC modelling

The ACIL Allen consultant report on wholesale energy cost estimate outlines the changes in contract prices and the modelled change in WEC for each distribution zone. The report notes that NSW contract prices have increased substantially, when compared with 2024-25 contract prices, in most quarters. Cap contracts have increased between 24% and 33% and Base contract prices increased by approximately 10% with the exception of Q3 which measured a 1% fall. We note the current methodology applies a 100% hedging cover for all profiles of the median of the annual peak demands across the 54 demand sets.

The estimated WEC percentage change for each distribution zone is forecast to be between 2.65% and 5.25%. This lower percentage change indicates there are WEC modelling factors that are materially tempering these contract price increases. We request the AER provide further guidance as to what additional factors are leading to the NSW WEC estimates in addition to the changes in contract prices.

The 'Solar Cost Adjustment'

The draft determination has proposed to incorporate a cost assessment that captures the observable costs arising from solar exports during periods of net generation which coincide with negative wholesale spot price events. In line with the initial proposal in the Issues paper, the AER has calculated an adjustment based on two modelled hedging strategies.

We support the AER exploring if this cost can reasonably be calculated under the current methodology. However the proposed adjustment demonstrates the significant complexity of forecasting a cost that is based on both future wholesale market dynamics that are rapidly evolving, and assumptions of a representative retailer's potential net generation capabilities. The hedging strategies derived from the current consultant modelling are based on a model focused on minimising spot price exposure from a traditional customer load, not of net generation exposure. This gives rise to challenges in considering if the current hedging model adequately reflects the retailer risks of a growing cost risk not considered when the model was created. Particularly as negative spot price events become more prevalent in the DMO based regions. Further, due to the limited transparency of the consultant's proprietary modelling, it is not clear how the different hedging strategies used to generate this result are determined, resulting in a lack of transparency as to how and why this additional risk results in a reduction in the measured wholesale costs

We disagree the AER's conclusion that it is not appropriate to address this issue by moving to the 95th percentile estimate of modelled cost outcomes. The paper states that a higher percentile estimate could overstate costs faced by retailers

We strongly disagree with this conclusion, as stated in our previous submission to the issues paper and prior DMO determination consultations. The movement to the lower 75th percentile estimate of modelled cost outcomes is contingent on confidence that the current methodology appropriately reflects all relevant wholesale cost drivers. If there is uncertainty as to whether these cost drivers are captured, the cost uncertainty should result in a more risk averse adjustment to the modelled scenarios considered when calculating the WEC.



The AER preference to transparently assess individual cost drivers when possible is appropriate. However, within the limitations of the current DMO framework, the proposed solar hedging adjustment demonstrates there may be significant challenges in deriving a transparent cost assessment that meaningfully reflects this type of market risk. In the absence of determining an industry accepted cost assessment, we consider it is appropriate to adjust the modelled cost outcomes to reflect a known wholesale cost that cannot be individually calculated. We acknowledge that a meaningful assessment may require fundamental changes to the DMO methodology and the regulatory parameters that guide the treatment of solar exports.

Retail Operating Costs

We support the AER's benchmarking approach to derive a representative retailer's operating costs and other costs based on actual retailer cost information. The weighted average approach strikes the right balance of reflecting the broad range of retailers participating in the market. As noted in the draft determination, this approach largely replicates the ACCC's requests in the Retail Electricity Inquiry.

The expansion of surveyed retailers is also an important evolution to the AER's methodology. This information is critical to informing the regulator as to the true costs faced by various retailers. As noted in the draft determination, the DMO cost assessment does not distinguish between standing and market offer customers when assessing costs retailers incur in serving, acquiring and retaining customers. This recognises the additional purpose of the DMO as a reference price and the impact on the competitive market, and also reflects the reality that retailer costs are not segmented into standing and market customers categories.

Retail Margin and Competition Allowance

Continued retail market pressures are leading to significant compression of publicly reported retail margins in most regions. Whilst the regulated price may aim to reflect a sustainable efficient margin for retailers, the reality is that many retailers face a significantly lower retail margin in the pursuit of customer growth and long term efficiencies. This market incentive is of benefit to all customers. If the regulated retail margin is set below an efficient return, this will undermine market competition and the benefits of long-term market efficiency. An appropriate retail margin is critical to support retailer viability and investment.

As outlined in the draft determination, retailer operating costs are increasing along with other cost components. In this context we support the AER's approach to apply a percentage retail margin to ensure retailer risks scale with the underlying costs. This is particularly important in light of increasing network costs and the recent rule change that restricts retail tariff reassignment when a default network tariff is changed. The regulatory requirement to preserve a customer's flat tariff structure when the underlying network charges change to a time of use tariff structure will require the retailer to manage this cost risk.

The draft determination has also proposed not to include the competition allowance. We do not support this decision however accept that the AER has decided its position based on the assessment that heightened cost of living pressures remain a significant factor for the AER determination. Whilst the draft determination notes that CPI had remained above the target band prior to December 2024, we encourage the AER to provide further guidance as to when the competition allowance may be included.

The competition allowance within the DMO is important to safeguard a balanced and sustainable electricity market that serves all consumers effectively. We support the re-introduction of the competition allowance as soon as possible.