Powershop Australia Pty Ltd. | GPO Box 1639 Melbourne, VIC 3001 | Phone 1800 462 668 | ABN 41 154 914 075

13 April 2026

Paul Harrigan
Executive Director, Default Market Offer and Consumers
Australian Energy Regulator
Melbourne VIC 3000

RE: Default Market Offer 2026-27 Draft Determination

About Shell Energy and Powershop in Australia

Shell Energy provides the energy businesses and households need for today and tomorrow.

A generation-backed trader and energy retailer, Shell Energy powers businesses and homes and acts as a catalyst to positively impact Australia's energy future.

We provide electricity, gas, and innovative solutions for our customers, complemented by our portfolio of gas-fired peaking power stations and battery storage assets, which support energy security and reliability.

Shell Energy is Australia's largest electricity retailer to commercial and industrial businesses, recognised for our market-leading customer service.[1] We offer business electricity, gas, and smart energy solutions. Our residential business, Powershop, provides greater choice and confidence to households and small businesses to help them take control of their energy through multiple energy plan options and digital tools.

Executive Summary

Powershop appreciates the opportunity to provide feedback on the Australian Energy Regulator's Draft Determination for the Default Market Offer for 2026–27 (DMO 8).

We recognise that the recent reforms to the DMO marks a shift in its role as a reference price and standing offer. We are concerned that the Draft Determination applies the new efficient cost methodology across the cost stack in a manner that materially understates the costs retailers incur. The Draft Determination reduces allowances across most elements of the cost stack, resulting in a DMO that does not reflect the efficient costs of supply in practice. Taken together, the revised approach to the DMO risks entrenching structural fragility in the energy retail market at a time of heightened macroeconomic volatility, accelerated energy system transition, and significant uncertainty.

Under the former "reasonable cost" framework, a modest degree of mismatch between modelled costs and real-world outcomes was tolerable. The Default Market Offer was designed to operate as a safety net rather than a precision pricing instrument, and some averaging across customer circumstances, tariff structures and operational constraints was expected. In that context, modest divergences between costs incurred and costs recognised did not undermine the integrity of the framework.

The shift to an efficient cost standard fundamentally changes this calculus. An efficiency-based framework requires that costs embedded in the DMO reflect outcomes that retailers can realistically (and reliably) achieve under the prevailing regulatory, physical and operational settings. It is our view that efficiency is inseparable from feasibility. The new framework has led the AER to assume actions of a hypothetical efficient retailer, without consideration of the feasibility of undertaking these actions. These assumed efficient actions across the cost stack, such as bulk network tariff optimisation, are outside the reasonable bounds of Rules or standard practise and are subject to external limitations, such as distributor processes or metering constraints. As a result, the assumed actions of an efficient retailer in the draft determination have resulted in a cost stack that retailers cannot reliably achieve given the constraints that limit the ability to optimise outcomes in the short term.

[1] Utility Market Intelligence (UMI) survey of large commercial and industrial electricity customers of major electricity retailers, including ERM Power (now known as Shell Energy) by independent research company NTF Group in 2011-2021.

The amended DMO framework requires the AER to determine prices based on the efficient costs of supplying customers, consistent with the National Energy Retail Objective of promoting efficient investment and operation of energy services. It is our view that efficiency in this context should not be assessed by seeking the lowest figures in abstract, line by line, in the cost stack.

While each individual adjustment to the cost stack may appear modest in isolation, the cumulative effect is persistent under-recovery across multiple cost components. In practice, the approach reflected in the Draft Determination places a disproportionate emphasis on short-term price outcomes, without sufficient regard to the long-term consumer interests that the Default Market Offer and the National Energy Retail Objective are intended to advance. This has resulted in a Draft Determination that prioritises near-term price reductions which may deliver transitory consumer benefits but does so at the expense of foundational conditions that are critical to sustainable, long-term consumer outcomes and central to an efficiency-based framework. These include market resilience, ongoing investability, and the prudent management of risk necessary to ensure reliable supply over time.

This submission focuses on the following key areas of concern:

- **wholesale energy cost settings**, including the risks of 50th percentile Wholesale Energy Cost (WEC) in volatile market conditions
- **network cost allowances** under the mandatory lowest tariff approach
- **retail operating cost allowances**, including bad debt and compliance costs
- **retail margin** and the treatment of investment and capital recovery

Current macroeconomic and geopolitical uncertainty increases the likelihood that energy supply costs across wholesale, network and retail components will exceed conservative point-in-time forecasts over the DMO 8 period, **heightening sensitivity to forecast error under a precision pricing framework.**

This may place upward pressure on wholesale outcomes through higher operating and maintenance costs, changes in bidding behaviour or increased outage durations, while transmission and distribution networks, particularly remote and regional assets, face similar cost drivers with potential flow through to network charges. Broader inflationary and financing pressures further compound these risks, increasing the likelihood that realised costs diverge from forecast allowances during DMO 8.

Powershop thanks the AER for the opportunity to provide comments on this matter. If you would like to discuss any part of this submission, please contact Brett Crossley at brett.crossley@shellenergy.com.au.

Yours sincerely

Libby Hawker

General Manager – Regulatory Affairs and Compliance

Wholesale energy cost settings

The Draft Determination signals the AER's intention to derive the wholesale energy cost (WEC) from the 50th percentile, supplemented by a volatility allowance. The AER has acknowledged that wholesale electricity prices are volatile and that retailers are exposed to this volatility when supplying customers, and hedging plays a critical role in managing that exposure and enables retailers to provide customers with stable prices over the life of their contracts.[2]

A central (50th percentile) allowance does not adequately reflect the risk profile retailers must manage in practice. Back-casting based on standardised hedging assumptions cannot replicate real-world hedging procurement or reflect prudent risk profiles of various retailers. As a result, reliance on a median estimate, risks understating efficient costs when markets are volatile or moving upward.

This matters because wholesale risk is asymmetric. Retailers face large downside exposure during price spikes but are not exposed to an equivalent potential benefit when prices fall. The consequences of under-recovery are therefore disproportionately severe, including material liquidity impacts, and those impacts are not evenly distributed across retailers given differences in scale or integration with generation, balance sheet strength, and access to hedging products

The shift to an efficient cost framework amplifies this issue. Each component is now set as a precise ex-ante allowance, with forecast error borne by retailers and no mechanism to true up under-recoveries in later periods. While an adjustment mechanism in subsequent DMO's could address forecast error in principle, adjustments applied in subsequent periods may arrive too late to prevent exit events, with consumers ultimately bearing the costs of market disruption and mutualised recovery.

Network cost allowances and mandatory lowest tariff application

A key challenge in the draft determination's approach to network cost allowances is the assumption that retailers can be assessed against the lowest applicable network tariff. This approach builds into the allowance a presumption that efficient retailers are able to standardise the underlying network tariff outcomes for their customers within each region. While this may theoretically represent a pathway to reduce network tariff cost allocations in the DMO and for retailers to limit exposure to network cost under-recovery against the DMO allowance, it presumes a level of control and optimisation over network tariff assignment that retailers do not possess during the DMO 8 period.

For small customers, network tariffs are set and reassigned by distribution businesses through their regulatory determinations and pricing proposals, rather than by retailers. Where tariff reassignment is feasible, retailers must obtain customer consent and submit a request to the distributor, which is assessed and approved or denied at the distributor's discretion. The National Energy Rules explicitly contemplate distributor driven tariff reassignment occurring independently of retail intent and after contract formation. Clause 6B.A3.2 of the National Electricity Rules requires a retailer to request that a distribution network service provider review a customer's network tariff where there is a change in expected usage such that the existing tariff may no longer apply. However, the decision as to whether a tariff reassignment occurs rests solely with the distributor, including whether to accept the tariff proposed by the retailer or to retain the existing assignment.[3]

This allocation of responsibility is reflected in the model terms and conditions for standard retail contracts. Clause 8.2(a)(4) provides that retailers must notify customers of tariff variations where those variations are a direct result of a tariff reassignment by the distributor pursuant to clause 6B.A3.2 of the National Electricity Rules.[4] The model terms do not provide retailers with any ability to control or override network tariff reassignment outcomes, but instead mandate the notification obligation to a customer once a distributor decision has been made. In practice, this means that even where retailers identify changes in customer usage patterns and request tariff reassignment, they remain dependent on distributor decisions. Retailers therefore do

[2] Australian Energy Regulator, State of the Energy Market 2024, Chapter 6.

[3] Australian Energy Market Commission, *National Electricity Rules*, clause 6B.A3.2 (Tariff reassignment)

[4] Australian Energy Market Commission, *National Energy Retail Rules*, Schedule 1 (Model terms and conditions for standard retail contracts), clause 8.2(a)(4).

not have unilateral control over ensuring customers are assigned to network tariffs that align with expected usage. There are additional constraints and unrecoverable costs created by the concurrent accelerated smart meter rollout which requires retailers maintain customer single-rate tariffs arrangements for a period following smart-meter install, unless consent is provided for a reassignment to occur.

Given that tariff reassignment requests are not guaranteed to be approved, and that approval rests with distribution businesses on a case-by-case basis, the draft allowance method systematically assumes outcomes that cannot be relied upon in practice. While there may be a sound case for reform to enable bulk tariff reassignment and improve alignment between incurred network costs and the DMO allowance, such reform would require a change to the Rules and sits outside the scope of the current determination and regulatory framework.

In the absence of such reform, applying a lowest tariff assumption structurally understates the network costs retailers must incur, even where retailers act efficiently and seek to minimise network cost exposure. Where customers cannot be moved to the lowest tariff due to distributor processes; is assigned a tariff that does not align to the network tariff due to restrictions placed unilaterally on retailers under the smart roll out; where there are metering constraints, or consent requirements, the resulting cost gap is unavoidable rather than discretionary. Excluding this unavoidable exposure from the DMO allowance risks producing a regulated price that does not reflect the efficient costs of supply and embeds systematic network cost under recovery within the determination itself, contrary to the intent of the amended DMO framework.

The draft network cost methodology is not cost-reflective. Our preference remains that the AER adopts a consistent, simple approach and use the corresponding network tariff to retailer tariff when setting network costs. Even then, under-recovery of network costs remains a live issue as the draft determination would not account for the tariff mismatches that are entrenched as part of ASMR obligations in DMO jurisdictions – reflecting the under recovery of networks costs in these circumstances is a live issue that remains unaddressed in the draft determination.

Retail operating cost allowances

In our response to the issues paper, Powershop emphasised the importance of cost reflectivity, transparency and competitive neutrality within the retail cost stack, noting that regulated prices must allow retailers to recover the efficient costs of supplying customers while maintaining appropriate consumer protections. At the same time, retailers face growing expectations to expand and deepen the support they provide to customers. Meeting these expectations requires ongoing investment in systems, digital tools and hardship and vulnerability frameworks, even as pressure to reduce costs and deliver short-term price outcomes intensifies. This creates a structural tension for retailers, where expectations continue to rise as the scope and complexity of regulatory and consumer obligations expand, but allowances within regulated prices move in the opposite direction. The cost of developing and maintaining compliant systems is therefore a growing challenge, particularly in the context of unprecedented regulatory change requiring substantial upgrades to systems and processes. In this new DMO environment, where costs are forecast conservatively in pursuit of efficient cost objectives, we urge the AER to consider the relationship between cost constraints built into the DMO cost stack and the level of scope this affords to go above and beyond the regulatory minimums to support energy consumers.

Bad debt

Bad debt allowances in the Draft Determination are derived from historical benchmarks and represent a forecast of expected future bad debt, rather than a mechanism for recovering actual bad debt incurred in prior periods. Under the efficient cost framework, any divergence between forecast and realised bad debt outcomes is borne entirely by retailers, with no opportunity for subsequent adjustment or recovery in later DMO periods. The AER has acknowledged that retailers are exposed to customer payment risk and that broader economic conditions materially influence bad debt outcomes. Where historical data are shaped by temporary government interventions, such as bill relief measures, or reflect materially different macroeconomic conditions, reliance on backward looking benchmarks risks understating forward looking bad debt costs. This risk is heightened in the current environment, where household financial stress, cost of living pressures and energy affordability concerns are increasing.

Instead of using historical bad debt reported by retailers to forecast future debt, it may be appropriate to use this data as a means to reconcile bad debt against the allowances built into the DMO over the same period. This would reduce the reliance on the AER to accurately forecast bad debt levels and provides avenues for actual cost recovery, which would be the most efficient and cost reflective outcome.

SSO cost recovery

We welcome the AER's decision to provide for cost recovery associated with the development and operation of the Solar Sharer Offer (SSO) in future DMO determinations. This approach recognises that the SSO is a mandated standing offer product that imposes new and material compliance, system and operational costs on retailers, and that these costs must be recoverable within the regulated framework.

This is particularly important given the nature of SSO costs. A significant proportion of SSO-related expenditure is incurred upfront and at the business level, including system builds, billing and settlement changes, training to uplift customer communications, and implementation of new compliance processes. These costs are largely fixed in nature and do not scale proportionately with customer numbers. For smaller retailers in particular, the cost to develop and operate a compliant SSO is likely to be broadly similar to that faced by larger retailers but must be recovered over a materially smaller customer base. Absent appropriate cost recovery, these obligations risk creating a disproportionate burden and undermining competitive neutrality.

We also note that the Draft Determination proposes to bundle SSO related costs within the SSO price framework. Greater clarity is needed on how these costs will be allocated and over what customer base they will be spread, particularly where customer uptake of the SSO may initially be limited. If recovery is constrained to a narrow cohort of SSO customers, there is a risk that fixed compliance costs cannot be efficiently recovered, particularly in the early years of implementation.

Retail margin

In seeking to infer the level of profit historically earned by retailers during previous Default Market Offer periods, the AER's approach to EBITDA analysis materially overstates realised profitability. The weighted average EBITDA observed the AER is 3.5% - this actual observed outcome falls well below the allowed retail margin benchmark built into previous DMO determinations. This reflects the fact that the cost stack and margin embedded in the DMO have, in practice, been insufficient to fully recover realised costs, with the "retail margin" component operated less as surplus profit and more as a buffer to manage cost overruns and volatility elsewhere in the cost stack. Excluding negative EBITDA outcomes rests on the explicit assumption that reported losses reflect inefficiency rather than deliberate, commercially rational investment decisions. This assumption does not reflect the commercial realities of energy retailing in Australia, nor the operating conditions faced by retailers during recent DMO periods.

At a time when retailers face unprecedented regulatory reform and accelerated market transition, retail margin settings should support prudent investment, innovation and sustainable participation in the long-term interests of consumers. Implementing an "efficient cost" framework while further compressing margins based on historical outcomes derived under a different regulatory regime, risks sending retailers the wrong signal about their role in the transitioning market. In particular, it may weaken the ability of retailers to invest in efficiency, innovation, and services that reduce consumer bills and improve the integration of consumer energy resources.