



Australian Government

**Department of Climate Change, Energy,
the Environment and Water**

Mr Daniel Harding
A/General Manager, Market Performance
Australian Energy Regulator

By email: DMO@aer.gov.au

Dear Mr Harding,

Re: Default Market Offer Net System Load Profile approach.

The Department of Climate Change, Energy, the Environment and Water (DCCEEW) welcomes the opportunity to provide a submission to the Australian Energy Regulator's (AER) Default Market Offer (DMO) Net System Load Profile (NSLP) Approach consultation paper.

First, we are supportive of the AER considering options for rectifying the issue identified in the SAPN and Energen datasets in the short-term, while the Australian Energy Market Operator (AEMO) implements a long-term solution.

I note that the NSLP is used by the AER as the 'representative load profile' for a retailers' residential and small business customers to calculate wholesale electricity costs as an input into the DMO. Whilst it is broadly representative, in practice, retailers are likely to hedge against their specific load profile that would vary depending on their customer base. The extent to which a precise representative load profile could be determined to reflect a retailer's hedging strategy is challenging.

Retailers consider a range of wholesale risk mitigation strategies, such as the ability to leverage vertical integration, power purchasing agreements, purchasing and storing their customers' solar exports or other types of bespoke contracts which are not considered as part of the wholesale cost methodology. The AER, in determining a suitable NSLP option, should consider the extent to which retailers will be sufficiently compensated for the risks they face.

Given the significance of the NSLP to determining wholesale electricity costs as an input into the DMO, and the issues raised by the consultation paper, a first-principles approach should be adopted for determining the appropriate dataset. A first-principles approach includes using a transparent and widely understood dataset such as AEMO's published dataset. Despite both options 1 and 2 using NSLP data from 1 October 2021 to 30 June 2023, option 2 requires a manual adjustment by ACIL Allen which decreases transparency, and reduces consistency between DMO determinations. Further, the ACIL Allen dataset does not reflect the load profile which retailers are likely to have been hedging against up until 1 October 2023, which is relevant to DMO6.

While it is incumbent on the AER to determine a DMO price level that best reflects the costs of supply consistent with a 'representative retailer' there are inherent complexities associated with this task that renders a precise outcome challenging. This objective should be balanced with a first-principles approach that utilises well known and established datasets, such as AEMO's NSLP.

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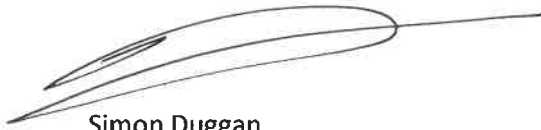
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I note the 2022 'Frontier Economics – review of wholesale energy costs estimation methodology' observed that the approach taken in DMO 1 to 4 had the potential to overestimate wholesale electricity costs. The extent to which retailers have previously benefitted from a conservative estimate of wholesale electricity costs at the expense of electricity consumers is a relevant consideration for DMO6.

As the AER notes in its consultation paper, the implications of using ACIL Allens dataset may result in materially different outcomes, with wholesale electricity costs 18 per cent higher in Energex, and 24 per cent higher in SAPN. This would translate to a material increase in retail electricity prices for impacted consumers at a time of significant cost of living pressures.

On this basis, I'd ask the AER consider adopting option 1 in preference to options 2 or 3.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Simon Duggan', with a long horizontal stroke extending to the right.

Simon Duggan
Deputy Secretary

23 February 24