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Default market offer prices 2025-26 – Issues Paper

Alinta Energy welcomes the opportunity to respond to the Australian Energy Regulator's issues paper on the Default Market Offer prices for 2025-26 (DMO 7).

Alinta Energy is an active investor in energy markets across Australia with an owned and contracted generation portfolio of over 3,300MW and more than one million electricity and gas customers and have been at the forefront of driving retail competition and delivering substantial benefits to consumers across competitive energy markets for many years. We make specific comments on questions raised in the issues paper below.

This issues paper identifies several issues impacting the variables that will be used to calculate DMO 7 prices. We understand that the AER is seeking to balance the objectives of consistency of approach over time while ensuring the DMO is as accurate as possible. We do not consider these objectives to be in competition with one another and can be pursued in tandem.

As discussed in previous submissions on the DMO method and approach, the setting of the DMO now involves a level of precision that departs from the original objectives of the DMO, which has resulted in historically low return on the risk and investment undertaken by retailers and reduced opportunities for innovation, competition and consumer choice. The bottom-up cost stack approach has required the AER to develop a focus on false precision which will never be able to replicate outcomes in the competitive retail electricity market. With the impact of consumer energy resources and a transitioning energy sector, the DMO needs to support, rather than hinder, investment in innovation and support consumer preferences.

Given this, Alinta Energy encourages greater flexibility in the AER's approach to DMO components given the current approach will be broadly retained for DMO 7. This includes re-adopting the 95th percentile of wholesale market outcomes for the calculation of wholesale energy costs and inclusion of the competition allowance given the downward trajectory of the consumer price index.

<u>An alternative model</u>

In previous submissions, Alinta Energy has put forward an alternative approach that would support the DMO objectives, while avoiding the complexity and risk associated with price regulation. It involves the AER setting a maximum percentage differential between individual retailer's standing and market offer prices. For example, if the value were set by the AER at 20%, retailers would be required to price their standing offer price no higher than 20% above any of their market offer prices. This simple method of price oversight would:

1. Eliminate the material risk of attempting to use regulation to identify an efficient price, which inevitably will be either too high or low;
2. Place competitive pressure on retailer's standing offer prices; and
3. Allow individual retailers to managing wholesale cost and other pricing risks in a manner that best matches their circumstances, their customers and their competitive strategy.

This approach would protect consumers from unreasonable prices (a retailer setting an unreasonably high standing offer price would be priced out of the competitive market) whilst retaining incentives for consumers to engage in the market (by permitting discounts in market offers of, in the above example, up to 20%).

To be clear, the AER would still be required to set a benchmark rate to enable price comparisons across retailers, where the benchmark rate would be used as a common base to compare retailer's prices. However, this benchmark rate would no longer perform the function of a universal standing offer. It could be calculated in a number of ways, for example as the median of all standing offer prices.

We would welcome an opportunity to discuss this model with the AER in more detail. Our subsequent comments in this submission are made on the basis that the current form of price regulation will be retained.

Alinta Energy would also welcome further discussion of any issues raised in this response with the AER, please contact David Calder (David.Calder@alintaenergy.com.au) in the first instance.

Yours sincerely

Graeme Hamilton
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Consultation questions

Wholesale costs Net System Load Profile and interval meter data

Question 1. Which option do you prefer and why?

Alinta Energy supports Option 2 to model the NSLP (one year of NSLP data to simulate the load profile blended with interval data).

In our view, applying Option 1 would not reflect the profile of customers who remain on the NSLP. While retailer-led deployment of smart meters has increased in recent years, many customers having smart meters installed are doing so through their investment addition of rooftop solar PV and other consumer energy resources. The characteristics of these small customers differ from customers whose meter is replaced as part of routine retirement or meter failure. As such, we do not consider Option 1 to be representative of the NSLP, whereby Option 2 should be adopted for modelling for DMO 7.

We note that ACIL Allens' blended approach to DMO 6 was more reflective of the variance in residential customer load than that ultimately use in DMO 6 and is similar to option 2 presented in the issues paper.

Question 2. Is there another available dataset that could be used to simulate the residential customer load profile that the AER is not currently considering? Is it publicly available?

Alinta Energy has previously provided the AER with load profiles on a confidential basis. While acknowledging the difficulty in using retailer's own load profiles as a basis to simulate residential customer profiles, we encourage the AER to compare its chosen profile with the actual profiles provided by retailers. Where material differences are identified, these differences need to be addressed.

Question 3. Do you have access to, or know of, any data which highlights the difference in the consumption profile of accumulation and interval meter customers, excluding the impact of solar exports?

As discussed above, retailers have their own data that demonstrates the difference in consumption patterns of customers with accumulation and interval meters. Household characteristics, size, location and other factors mean that interval-only data is not, at this stage, representative of customers who remain on accumulation meters (who still constitute the majority of customers covered by the DMO).

Question 6. Given issues with the available load profile data, should the AER determine separate load profiles and associated wholesale cost forecasts for residential and small business customers? Are there factors we should consider, depending on which load profile data option is used?

Alinta Energy believes that the AER should determine separate load profiles and the resulting WEC for residential and small business customers. The load characteristics of residential and small business customers varies significantly and a more accurate WEC could be determined for both classes of customers if separate profiles were applied.

Controlled Load Profile (NSW)

Question 7. Which option do you prefer and why?

Alinta Energy recommends adoption of Option 2 on the grounds that it would be consistent with Option 2 for the NSLP. Option 3 would exclude CL customers with accumulation meters, a significant subset of customers in NSW. Option 1 may create a disconnect with settlement of CL customers.

Solar PV exports and hedging costs

Question 14. What are your views on whether the AER should consider accounting for any additional hedging costs arising from customers' solar exports? If you are a retailer, how does the presence of customers' solar exports impact your hedging strategy and how could these additional costs be quantified within the wholesale methodology?

Alinta Energy supports the AER accounting for additional hedging costs associated with customers' solar exports. We appreciate the difficulty in developing a proxy for this as rooftop solar PV continues to expand. A proxy measure involving the difference between a profile including solar exports and one excluding with the difference a reflection of the hedging costs for solar exports as discussed on page 22 of the issues paper.

South Australian wholesale methodology

Question 15. Further to analysis of OTC contract information, are there other methodologies the AER could investigate to benchmark wholesale cost forecasts in South Australia?

Alinta Energy supports the continuation of the approach adopted by the AER for DMO 6, including the analysis of confidential OTC contract data.

Question 16. Should the AER repeat the LRMC analysis for DMO 7 as a comparative data point for wholesale energy costs in South Australia?

The South Australian Government is considering policy options to support the high penetration of renewable energy in its jurisdiction. We question the value of LRMC analysis that resulted in lower WEC estimates than the AER's current methodology and how this would support competition and liquidity in the South Australian retail electricity market in the longer term.

Retail costs

Question 19. Do you consider these current methodologies appropriate and, if not, what alternatives should be considered?

We support the AER obtaining its own retail costs information from as broad a cohort of electricity retailers as possible. This will be more reflective of actual retail costs and the costs incurred by smaller retailers competing in the market.

Retail margin and allowance

Question 21. Do you consider the proposed retail margins appropriate and, if not, what alternatives should be considered?

As discussed above, we do not consider the proposed returns for the risk and investment made by retailers for DMO 7 to be appropriate, which includes the basis for excluding the competition allowance. We believe that applying the competition allowance, based on the declining CPI, be considered for DMO

7 to support competition and consumer choice. The state of electricity retail market competition is one factor to consider, but the sustainability of a viable competitive market in energy will ultimately serve the long-term interests of consumers.

> Question 22. What is the most appropriate approach to incorporating a diverse range of retailer costs to serve in DMO prices?

As discussed in our response to question 19, we support the AER collecting data from as broad a cohort of retailers as possible to obtain a transparent and realistic view of the cost retailers face to participate and compete for customers. These costs include an ever-growing regulatory burden that diverts resources from investment in innovation in product offerings and improving customer's experience in the energy market.

> Question 23. What other factors, if any, should the AER consider in deciding whether to apply the competition allowance?

See our response to question 21 above.

Other DMO costs and considerations

> Question 24. Should network costs be based on a blend of flat rate and time of use network tariffs and why or why not? How could the issues above be overcome – particularly for small business network tariffs – if we were to create a blended cost?

In our response to the DMO 6 issues paper, we acknowledged the difficulty involved in blending flat and time of use network tariffs and the transparency associated with this approach.[1] The AER lists numerous challenges associated with blending flat and time of use network tariffs and weighting these to determine the network use of system component of the DMO.

Given the recent decision by the Queensland Government requiring retailers to make available a flat retail standing offer to all customers and a similar obligation proposed by the Australian Energy Market Commission[2] (including additional explicit informed consent provisions), the AER needs to consider the additional costs incurred by retailers by the mismatch between network tariffs and the retail tariff structure. The former will be levied by distributors on a demand or time of use basis, with the latter constrained to a flat structure. Retailers are unable to hedge against network tariff risk that may result from the pattern of use of their customers, the price signal will not be communicated to customers and behaviour will not change as a result.

While further increasing the already complex calculation of the DMO, there may be a need to set DMO prices for different network and retail cost-reflective tariff types on a stand-alone basis over time. It also provides further justification for Alinta Energy's alternative model for setting standing offer tariffs, as outlined above.

> Question 25. What are your views on whether the AER should consider adopting new annual usage amounts? What alternative sources should be considered, and/or what values would be more broadly representative than the current assumptions?

To the extent that annual usage amounts for small business customers are understated, if the AER intends the DMO to accurately reflect consumption levels, there is merit in examining a change to the

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[1] Alinta Energy (2023), *Submission to the DMO 6 issues paper*, page 8.
[2] AEMC (2024), *Accelerating Smart Meter Deployment – Directions Paper*, page iii.

assumed values. Applying a single representative annual consumption further demonstrates the difficulties of determining a reference price through regulation. The AER notes that comparisons may be difficult to make if a higher annual consumption figure were adopted for DMO 7; applying a figure that does not reflect the consumption levels of small business customers is also of questionable value.

Question 26. What benefits do you see in further consideration of improvements to the methodology of timing and pattern of supply? How material may this be and how could we address any additional complexity it causes?

As for annual consumption levels, the timing and pattern of supply should be as accurate as possible. By allocating consumption in a way that effectively flattens the profile of consumption does not serve the long-term interests of consumers. We would welcome further consultation with the AER on any changes to the approach to determining the timing and pattern of supply and any complexities that a change may introduce to retail pricing. Fundamentally, the approach should reflect actual outcomes and not artificially amplify or mute consumption patterns.