01 April 2025

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Sent via email to: DMO@aer.gov.au

Re: Default Market Offer Prices 2025-2026

I refer to your Default market offer prices 2025-26: Draft determination paper (DMO 7) and thank the Australian Energy Regulator (AER) for its consideration of stakeholder views.

1st Energy is a non-integrated, second-tier electricity and gas retailer serving customers across New South Wales, Queensland, South Australia, Tasmania, and Victoria. Since our establishment in 2015, we have been committed to offering competitive energy products in an increasingly complex and evolving market.

The rising cost of living remains a significant concern for Australian households. As Treasurer Jim Chalmers recently acknowledged, "Australians are under pressure. That is still the case. Even though we have made very substantial progress together on inflation and now sustained progress on inflation, we know that Australians are still doing it tough and that's why the cost of living is the Albanese government's primary focus.[1]" This reality is reflected in our own interactions with customers, who are increasingly looking for meaningful price relief.

We recognise that energy ministers have called on the AER to review costs as part of the DMO process. However, it is crucial that this does not result in artificially lowering prices in a way that undermines the integrity of the framework. The AER has access to financial data from 26 retailers, and this data should be accurately reflected in the DMO 7 determination. Ensuring the price remains cost-reflective is essential for maintaining a sustainable and competitive energy market that continues to function effectively for all customers.

While the DMO is designed as a safeguard for customers who do not engage in the market, it is important to ensure that it does not inadvertently set a benchmark that discourages competition or innovation. A well-functioning retail market relies on the ability of retailers to offer diverse and competitive plans that cater to different customer needs. Striking the right balance between protection and market efficiency is critical to ensuring the long-term benefits for consumers.

Additionally, we continue to advocate for stronger support mechanisms for vulnerable customers, including well targeted assistance measures such as the Energy Bill Relief Fund and the ongoing provision of relief schemes.

Further details on our position in response to the AER's draft determination can be found in **Appendix A**.

For any queries regarding this response, please contact Aneta Graham, Head of Regulatory and Compliance, aneta.graham@1stenergy.com.au.

Yours sincerely

Liam Foden
Managing Director
1st Energy Pty Ltd

[1] https://ministers.treasury.gov.au/ministers/jim-chalmers-2022/transcripts/interview-natarsha-belling-national-news-noon-channel-7

Appendix A

Network costs

Through its draft determination the AER has chosen to maintain its existing approach of using a flat rate network tariff to determine network costs, despite receiving mixed feedback from stakeholders. Whilst this approach provides continuity for the current determination, we believe a blended approach should be given significant consideration moving forward, particularly in the context of the current evolving tariff landscape. With the commencement of the accelerated smart meter rollout, the shift towards time-of use tariffs is becoming increasingly important. However, there is a growing mismatch between network tariff structures and the flat rate tariffs retailers are required to offer moving forward.

Networks are empowered to progressively shift their cost bases to reflect more dynamic pricing, yet retailers remained constrained by the flat rate tariff structure unless customers provide explicit informed consent to move to a cost-reflective tariff. To ensure the DMO remains fit for purpose, we strongly encourage the AER to closely monitor the impact of smart meter deployment on network pricing and retail offerings. It is critical that network costs within the DMO accurately reflect what networks are doing in practice. Obtaining direct network cost data is essential, even if it introduces additional complexity, to ensure that pricing structures remain aligned with real-world costs and market transitions.

Wholesale costs

We acknowledge the AER's position that, under the approved DMO methodology, small customer solar exports cannot be included in the interval meter dataset as the DMO is designed to reflect the price charged by retailers for customer imports. However, we continue to hold the view that excluding solar PV impacts entirely overlooks a fundamental shift in market dynamics, particularly in relation to negative load and negative spot pricing exposure for retailers.

As we previously highlighted, solar PV output significantly alters consumption patterns, reducing net customer load during the day and pushing negative spot prices. This is resulting in spot pricing exposure to retailers because when net load and spot prices are negative, we're exposed to spot price outcomes and must make payments to AEMO. The result is a material financial risk that is not adequately accounted for within the current DMO framework.

Furthermore, we note that the AER's solar hedging adjustment has, in most cases, resulted in lower cost allowances, except in one distribution area. This outcome suggests that the adjustment does not fully account for the real costs imposed on retailers by negative spot pricing events. We have previously provided data demonstrating these cost impacts[2], yet they appear to have been disregarded in favour of an approach that assumes no material financial burden on retailers.

We acknowledge that the AER has sought to address this issue through a solar hedging adjustment however, we remain concerned that alternative strategies suggested by the AER to manage retrospective load variations do not provide a practical solution for all retailers. The suggestion that retailers can offset these impacts through feed-in tariff adjustments, hot water control, electric vehicle charging orchestration, or demand management programs assumes a level of influence over customer load profiles that retailers do not necessarily have. These mechanisms may be relevant to network operators or policymakers, but they do not provide a practical or immediate cost-recovery solution for retailers. The AER's suggestion that retailers can simply choose not to engage with solar customers is both inappropriate and impractical. Excluding a growing segment of the market – one that government policy actively encourages through solar incentives and support schemes – would neither be commercially viable nor in the interests of consumers. Retailers cannot and should not be expected to disregard an entire customer group simply because the current DMO methodology fails to account for the real costs associated with solar exports.

Whilst we recognise the need for methodological consistency in wholesale cost calculations, we urge the AER to continue exploring alternative ways to ensure that retailers are not unduly exposed to negative spot price

[2] Confidential 1st Energy AER Draft Determination Default Market Offer Submission April 2024 Appendix B

outcomes driven by solar PV exports. This could include enhanced hedging cost allowances, or a broader review of how solar-driven market distortions are factored into retail price regulation. Given the increasing penetration of distributed solar and it's continued impact on market conditions, this issue will only increase in significance, and it is imperative that future DMOs reflect these evolving cost pressures in a way that is both transparent and equitable.

We continue with the view that a 95th percentile hedged wholesale energy cost estimate remains appropriate and reflective of a prudent retailer and is the appropriate mechanism currently to address the risk faced to retailers for solar hedging costs. Rystad Energy says a comparison of 39 electricity markets globally reveals that Australia's NEM has the widest spreads between high and low wholesale electricity prices over the course of each day, giving it "the unwanted title of 'most volatile'."[3]

Competition allowance

As with the DMO 6 the AER have determined that it is appropriate, due to economic conditions, to exclude the competition allowance, citing ongoing cost-of-living and pricing pressures. However, while the AER has noted CPI movements remain uncertain, we believe there should be greater clarity on how CPI is assessed in this context, particularly given many stakeholders have raised concerns about the interpretation of when CPI is considered materially above the RBA's target band.

Additionally, the AER has attributed that recent reductions in electricity prices have been driven in part by government energy bill relief, which is expected to end before the onset of DMO 7. However, the Australian Government has announced a $1.8 billion extension of the Energy Bill Relief Fund by six months in the 2025–26 Budget[4]. Given this extension, the use of the trimmed mean CPI now seems inappropriate. We support the AER's commitment to reassessing its position once the ABS March 2025 CPI data is available and strongly advocate for the use of headline CPI as the appropriate measure. Furthermore, we note that the issues paper did not reference the trimmed mean CPI, yet it has now been introduced as the metric under consideration. This late inclusion raises concerns about its appropriateness and transparency, given its potential impact on pricing outcomes.

[3] https://www.rystadenergy.com/news/australia-electricity-market-most-volatile-in-the-wor
[4] https://www.energy.gov.au/energy-bill-relief-fund