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Department for Energy and Mining

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DEMC24/01535

Ms Natalie Elkins
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Dear Ms Elkins

Default Market Offer prices - 2025/26 Draft Determination

The South Australian Department for Energy and Mining (DEM) thanks you for the opportunity to comment on the Default Market Offer (DMO) prices – Draft Determination.

The South Australian Government remains committed to reducing consumers' electricity bills and thanks the Australian Energy Regulator (the regulator) for its work on the 2025/2026 DMO determination.

DEM is concerned the draft determination will negatively impact South Australian consumers in the upcoming financial year, should the decision be implemented. We urge the regulator to further consider the broader cost-of-living pressures consumers are currently facing as it develops its final determination.

The regulator's recent retail performance report for Q2 of 2024/2025 shows that, by many measures, electricity customers are struggling in the current economic environment.

The proportion of customers in energy debt and the average amount of that debt are both rising, with the latter increasing by $383 over the past year for residential customers. The average debt of customers on hardship programs and the debt at entry to these programs have also continued to grow. Although disconnections have decreased in recent months, they remain higher than a year ago. The government's Energy Bill Relief package has likely prevented these numbers from being even higher.

This is all despite median market offers for electricity falling from the beginning of July until 31 December 2024. The regulator's preliminary analysis of prices at 1 February 2025 further indicates the gradual decline in prices from mid-2024 has continued.

The report also shows that tier 2 retailers continue to gain more market share, which indicates increased competition in the retail energy market, and that the level of the current DMO has enabled smaller retailers to compete.

This suggests that the significant increase in retailer operating costs across jurisdictions could be adjusted down and the objectives of the DMO still be met. While we acknowledge the additional information collected from smaller retailers, most of this increase has been from larger retailers that have increased spending on hardship programs, debt collection and customer acquisition and retention. The regulator's draft decision notes that retail and other costs for these larger retailers increased between 25% and 31% for residential customers, depending on the DMO region.

While acknowledging the importance of including retailers' cost to serve customers in the DMO, and supportive of the additional assistance provided by some retailers to those in hardship, we do question the peculiar cycle that has been created. Increasing prices being driven by rising customer acquisition and retention costs will cause more customers to struggle with their energy bills. This then leads to retailers spending more on meeting the needs of these customers or chasing debt. As all these additional costs are allowed to be recovered by retailers, prices increase further, placing more pressure on customers.

The draft determination shows that a considerable range exists in the various retailers' costs to acquire and retain customers, and that a number of smaller retailers have costs lower than the weighted average of the big 3 retailers. This suggests that some retailers could potentially manage higher acquisition and retention costs through better operational efficiencies or innovation. It is also unclear why around $10 per customer is allowed to be recovered by 'other' costs to acquire and retain customers, over and above the expected labour, advertising and customer onboarding costs. We therefore question whether alternative cost-saving measures or strategies would help mitigate the impact of rising customer-related expenses without raising prices for consumers, which then leads to additional retailer operating costs.

While only a small factor in the DMO increase in South Australia, it is also surprising that retail costs associated with bad and doubtful debts have increased despite recent government subsidies. We encourage the regulator to investigate stakeholder concerns about the distinction between actual bad and doubtful debts incurred by retailers and estimates, to ensure the inclusion of these costs in the DMO remains appropriate.

It is encouraging that retailers are still offering prices well below DMO 6, despite the current DMO price not including a competition allowance. DEM's analysis, as of mid-March, shows that there are currently around 91 offers for residential customers (of the total 129 on EnergyMadeEasy) below the current DMO, with many more at the DMO level. For small business customers 42 offers out of 69 are below the DMO.

For this reason, we continue to oppose the introduction of a competition allowance in DMO 7. Its exclusion from DMO 6 did not result in a contraction of the energy market as suggested by some parties. We therefore consider adding a competition allowance would be completely inappropriate in the current environment.

DEM acknowledges the regulator's further analysis to determine if the retail margins from DMO 6 remain appropriate. Notably, the retail margins for the final DMO 6 determination were above the midpoints between the lower and upper bounds of the regulator's estimates of efficient margins. This was particularly the case for South Australian small businesses and residential customers without controlled load.

We consider that there is an opportunity to provide a better outcome for consumers through reducing the retail margins from the 6% and 11% proposed by the regulator. This is particularly the case given the increase in the dollar value of margins in the draft determination of between 2.5% and 8.9% for residential customers and between 4.2% and 8.2% for small businesses.

It is also noted that the Victorian Essential Services Commission has reduced the retail operating margin to 5% of the total Victorian Default Offer cost stack in its draft determination, down from 5.3% in 2024/25. The Commission notes that this change acknowledges the importance of a reasonable return for retailers while also offering some relief to customers facing cost-of-living pressures. The regulator could consider applying a similar approach.

DEM has also previously noted that applying a retailer margin on a percentage basis will compound increases in other components of the DMO, resulting in a larger increase than may otherwise be the case. We were interested in the views of Frontier Economics during their engagement on the Independent Competition and Regulatory Commission's Retail Electricity Prices determination for ActewAGL customers for 2024-27. They stated that applying the retailer margin as a percentage ignores that increasing energy costs *reduce* the risk faced by the retailer and so therefore overcompensates the retailer as energy costs increase. While they also noted that applying a dollar value may undercompensate retailers, they therefore proposed a hybrid solution. This is an alternate approach the regulator could consider.

Regarding wholesale costs, while price increases in 2024 were driven by large increases in the third quarter due to several high-priced events, it is hoped that the significant drop in average spot prices in the fourth quarter 2024 and into 2025 will continue.

Base and cap futures prices monitored by the Department for the DMO 7 period have decreased over the past 18 months. Apart from the increase in mid-2024, there has been a steady decrease through to March 2025 that we hope is reflected in the trade weighted data used in the final determination.

In summary we strongly urge the regulator to consider broader economic conditions and cost-of-living pressures as it develops the final DMO determination.

DEM thanks the regulator for the work on this important determination. Should you have any questions in relation to this submission, please contact Mr Chris Leverington, Senior Policy Officer, Strategic Policy and Delivery Division, on (08) 8429 3298.

Yours sincerely

Rebecca Knights

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