AUSTRALIAN ENERGY COUNCIL

Ms Electra Pappas

Acting Branch Head

Electricity Markets

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

GPO Box 3090

Canberra ACT 2601

28 July 2025

Dear Ms Pappas,

Reforms to the Default Market Offer

The Australian Energy Council (AEC) is the peak industry body for electricity and downstream natural gas businesses operating in the competitive wholesale and retail energy markets. AEC members generate and sell energy to over 10 million homes and businesses and are major investors in renewable energy generation. The AEC supports reaching net zero by 2050 and a 55 per cent emissions reduction target by 2035 and is committed to delivering the energy transition for the benefit of consumers.

The AEC welcomes the opportunity to submit to the Commonwealth Department of Climate Change, Energy, the Environment and Water's (DCCEEW's) consultation on reforms to the Default Market Offer (DMO Review). The AEC is a strong supporter of the view expressed by Energy Ministers that "strong consumer protections are fundamental to the community's trust towards energy transformation".[1]

We provide a detailed submission in the following pages. In summary, we:

- Believe the difference between the DMO and VDO outcomes is due to different wholesale and network costs
- Found that the DMO and VDO methodologies are largely similar
- Consider that the current indicative direction of energy costs is upwards in the medium term, primarily due to rising wholesale and network costs
- Urge DCCEEW to closely consider the unintended consequences that could arise for consumers from stricter price controls and a framework that results in the DMO being set too low

[1] https://consult.dcceew.gov.au/better-energy-customer-experiences

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- Support real opportunities to lower retail prices, with a focus on measures that improve productivity, such as removing duplication by having only one energy regulator
- Encourage development of a pricing framework which caters to the different needs and values of customers, and believe this is only likely to evolve if reforms identify and target customer cohorts from a spectrum of least to most engaged
- Highlight the value of retail market competition for the cost to serve and product differentiation benefits, and because it also supports investment in generation through wholesale contracting and hedging strategies, as assumed by the Wholesale Markets Review.

Likely drivers of energy costs between now and 2030

The attached report from Ernst & Young (the EY Report) was commissioned by the AEC and provides analysis on the implications of the proposed reforms to the DMO (see Attachment 1). The EY Report compares DMO and VDO price setting principles, methodologies and outcomes. The EY Report finds that the difference between the DMO and VDO outcomes is most likely due to different wholesale and network costs:

> *"Despite both methodologies being largely similar, particularly while the competition allowance hasn't been included in the DMO, the average residential DMO is $647.00 higher than the VDO for 2025-26. This is most likely due to the average wholesale and network cost being higher across NSW, SEQ and SA than it has been across Victoria."*[2]

There are underlying pressures on energy costs, and the AEC considers that the current indicative direction of travel is upwards in the medium term, even if the DMO Review recommends changes to the DMO methodology for determining retail costs. The EY report notes that while the Australian Energy Market Commission 10 year outlook for residential electricity prices projects all cost components would decrease over the next 10 years, it assumed that the anticipated increase in renewable generation in AEMO's ISP is delivered efficiently and on-time, and also that Consumer Energy Resources (CER) are effectively integrated in a timely and efficient manner:

> *"Recent announcements regarding key transmission projects in AEMO's ISP suggest that the assumptions about timely and efficient connection of new generation are at risk of not being realised, which could in turn delay the downward pressure on energy prices beyond the 10-year horizon. For example, AEMO recently announced a two-year delay in the key VNI West transmission project, and delays and increased cost to other key projects such as Project EnergyConnect. The estimated cost of VNI West has increased by $1.7b, from an estimated*

[2] Ernst & Young (2025) 2025 Reforms for the Default Market Offer, p.7 – attachment 3 of this submission

$1.6b in 2023 to $3.3b today, and EnergyConnect is expected to cost $1.5b more than originally estimated."[3]

The EY Report also notes that "the successful deployment of widespread CER orchestration is likely to take several years to realise"[4] and that "if delays in building the required transmission and generation assets persist, it is likely to lead to increased network and wholesale costs, which are the main components of energy bills.".[5]

Echoing concerns from Ernst & Young, the Ai Group recently released analysis highlighting that if energy productivity is low, and in particular, the buildout of transmission, generation and storage is delayed or at avoidably high cost, then prices overall would be impacted:

"If new transmission, generation and storage projects cannot be built, or are built at avoidably high cost, everyone will pay higher bills; endure worse reliability and be exposed to more of the serious long-term consequences of climate change."[6]

Increasing price controls on retailers risks unintended consequences

Experience in the United Kingdom illustrates some of the unintended consequences of strict retail price caps, as outlined in the EY Report. These can include:

- "Additional costs and risks as a side effect of the cap design, including supplier failure during extreme market volatility"[7]
- "Impacts on competition, innovation and service levels over time as a result of the existence and design of the cap. Ofgem notes it is important to consider adverse effects on consumers if the cap reduces incentives on suppliers to offer more competitive prices or to offer better services through improved efficiency and innovation."[8]
- "The growing challenge of applying the cap to an increasingly diverse market, especially when considering growing bad debt levels. Ofgem notes a stringent one-size-fits-all cap may create challenges for some suppliers that have higher cost to serve customers than other suppliers."[9]

Likewise, in addressing the issue of the "loyalty penalty", the EY Report refers to a study by the University of New South Wales, which "cautioned that well-intentioned policies to ban loyalty penalty

[3] Ibid p.8
[4] Ibid p.11
[5] Ibid p.11
[6] Ai Group (2025) Energy: More, Faster, Cheaper at https://www.aigroup.com.au/news/policies/2025/energy-more-faster-cheaper/ p.7
[7] Ernst & Young (2025) op cit p.13
[8] Ibid p.13
[9] Ibid p.13

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practices (e.g. by limiting the price differential between new and existing customer markets) could have unintended consequences that could potentially cause more harm to customers than good."[10] The AEC believes that addressing this issue risks taking away the very market that currently provides low-cost offers to the majority of customers and is the gateway for lowest cost optimisation and integration of CER.

In both of the above price control measures (strict retail price caps and addressing the "loyalty penalty"), the EY Report illustrates that regulators have undertaken lengthy inquiries and evaluations because of the scope and scale of unintended consequences that can arise. Given the very short timeframes of the DMO Review, the AEC urges DCCEEW to contain its decisions in the DMO Review to areas where unintended consequences would be limited in terms of scope and scale.

Customer impacts of setting the DMO too low

The DMO and VDO only apply to a minority of customers on standing offers – the majority of customers are on market offers below the DMO/VDO. In 2025, there were 8.2% of residential customers on the DMO and 12% of residential customers on the VDO.

The AEC believes that competition, not regulation, is the most effective long-term mechanism to drive down prices and improve service. All consumers benefit from effective retail competition. This benefit also accrues to those consumers who do not participate frequently and remain on, or close to, standing offer prices. Firstly, because they *can* access a market offer at any time. Details of better offers are now shown on all bills in NECF jurisdictions, and this has been demonstrated to be effective.

Secondly, competition creates a strong incentive for retailers to minimise all the costs in their cost stack. This includes their cost to serve and other operating costs, bad and doubtful debt costs, and environmental and wholesale costs. This does flow through to the DMO, since retailers report actual costs to the AER, and the AER uses this information to set regulated allowances.

Finally, the direction of policy and market reform outside the DMO framework and within the Wholesale Markets Review is important to understand and the relevance of the DMO should be considered within that broader framework, which assumes the preservation of incentives for retail market competition. Retail competition not only has cost to serve and product differentiation benefits, it also supports

[10] Ibid, p.15

generation investment: retail competition supports wholesale contracting and hedging strategies, including small generation and batteries, all of which deliver benefits to all consumers.

Smaller retailers, in particular, play a critical role in stimulating competitive pressure by targeting disengaged customers of larger incumbent providers. For these participants to compete effectively, they must be able to recover the costs associated with customer acquisition and earn a reasonable return.

In considering the competition allowance, it is important to recognise that individual retailers face differing cost structures, which may not align with the benchmark assumptions underpinning the DMO and VDO methodologies. For example, smaller new entrant retailers are particularly vulnerable to higher wholesale costs. We observed this during the energy crisis in 2022, when there was an unprecedented number of Retailer of Last Resort events.

The EY Report outlines the risks for customers and retailers of setting the retail margin too low:

> *"If the margin is set too low and there is no allowance for competition, it could make the market less attractive for new market entrants and lead to existing retailers exiting the market, leading to less choice and an absence of competitive tension to put downward pressure on prices. Additionally, it could also lead to reduced incentives for retailers to develop innovative products and services, including those that would encourage greater level of orchestration of customers' CER.*
>
> *If the incentive to compete is reduced, it will lead to less choice and therefore less incentive for customers to engage in the market."*[11]

Real opportunities to lower retail prices

The EY Report outlines the potential consequences of removing a competition allowance and finds a modest impact due to the nature of the cost stack:

> *"While permanently excluding the competition allowance would reduce the overall DMO prices, it is unlikely to have a material impact because it is a small component of the bill compared with wholesale and network costs."*[12]

In contrast, there are several reform options not considered in the DMO Review consultation paper which could deliver ongoing and tangible reductions in retail prices, including:

[11] Ernst & Young (2025) op cit p.12
[12] Ernst & Young (2025) op cit p.12

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- Removing the current regulatory duplication created by having two energy regulators (the Australian Energy Regulator and the Essential Services Commission). The AEC considers this reform option offers potentially significant productivity benefits.
- Remove some of the prescription currently in the energy laws, rules and regulations in line with the move to a more principles-based regulatory framework.
- There is significant value in supporting distribution network businesses to send simpler, more effective price signals to retailers to unlock further value and support retailers to better incentivise customers to participate in virtual power plant offerings, making these programs increasingly scalable. This will help to ensure distribution network capacity is better utilised without unduly penalising customers, particularly those that cannot afford to access CER.
- An improved focus (and faster action) on CER interoperability frameworks to enable consumers to easily switch service providers and participate in markets would be highly beneficial and support the recommendations arising from the Wholesale Market Settings Review.
- A broad review of the National Energy Consumer Framework to simplify and align obligations across jurisdictions, reduce cost and improve the customer experience.

The AEC supports the above options being tabled for further exploration.

Keep it simple: an efficient price framework application should only apply to relevant customer segments

The AEC believes that it is worth considering whether the scope of the DMO should be narrowed to focus on the segment of customers that have the most difficulty engaging in the market (or actively choose not to engage). Another area worth investigating is whether the DMO could be a flat tariff only, with networks required to revert any DMO customer to a flat price. In line with our advice above related to the short timeframes of the DMO Review, the AEC supports consideration of these options for reform as part of a lengthier review process. The AEC is an active participant in the AEMC Pricing Review consultations and will continue to contribute these and other ideas to that process.

Price frameworks should support customer choice and engagement on innovative or value-add products and services

Regulatory frameworks are not keeping pace with the rate of technological change in how customers consume energy and the DMO/VDO are good examples of this. A volumetric tariff reference price provides little value for more engaged customer segments, given these customers are engaging in CER or other technologies that make comparisons with a volumetric reference price redundant. While we recognise the role of the reference price for some offers, this does not accommodate emerging

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proposition models such as subscriptions, dynamic tariffs, or offers that reward flexible demand; yet these are increasingly relevant as the system decentralises.

The AEC believes we need a fit-for-purpose exemption framework for retailers offering products that fall outside the standard DMO/VDO constructs. For example, CER or subscription-based offers may be subject to rigid price comparison and contract disclosure obligations that were not designed for these models. An automatic and established exemption framework could allow for regulatory flexibility while maintaining core protections.

The AEC also supports the development of tailored, transparent comparison tools (e.g., online calculators that model actual usage patterns or customer CER profiles) to help and encourage customers to see the true value of dynamic and non-volumetric offers.

This submission is informed by our Future Role of Retailer project

Since November 2023, the AEC has been embarking on a long-term project focused on the needs and values of customers now and into the future as the energy market evolves to a high Consumer Energy Resources (CER) environment.

AEC retail members have been part of the energy system evolution, providing customers with rooftop solar and battery offerings, virtual power plans, and EV bundles and EV charging plans. Our members are also working with other industry partners on current trials to test new technologies and innovative pricing arrangements that could deliver better outcomes for customers in the future.

We have developed a CER Integration strategy to provide a structured and holistic approach to guide our consideration of the changes to industry arrangements needed to serve customer needs in the future system. As part of this strategy, we initiated the *Role of Retailer* project and have worked with our retail members to identify customer needs and values and consider what products and services customers may need in the future system and the changes that may be needed to retailers' role to deliver the outcomes customers require. This submission draws on the insights we developed through the first phase of the project (refer to Attachment 2 for more details on this project).

The Role of Retailer project is still ongoing. We continue to consult with stakeholders on findings in 2025 and welcome the opportunity to work with DCCEEW to further refine our thinking on the future role of the retailer.

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We welcome opportunities to work closely and iteratively with DCCEEW

Recent past reform efforts that were successful heavily relied on open and consultative processes where a broad range of stakeholders collaborated to stress test and improve recommendations and solutions. We support DCCEEW taking a similar approach, and we welcome opportunities to meet with DCCEEW to discuss our Role of Retailer project as it relates to the DMO Review.

The AEC has responded to the specific consultation questions in Attachment 3. We list our recommendations overleaf.

Please do not hesitate to contact Jo De Silva, GM Retail Policy at jo.desilva@energycouncil.com.au or by telephone on 0406 950 726 if you wish to discuss this submission further.

Yours sincerely,

Jo De Silva

Jo De Silva

General Manager Retail Policy

David Markham

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AEC Recommendations

Number	Recommendation
Options for retail price reductions	
1	Table the following reform options not considered in the DMO Review consultation paper which could deliver ongoing and tangible reductions in retail prices, including: • Removing the current regulatory duplication created by having two energy regulators (the Australian Energy Regulator and the Essential Services Commission). The AEC considers this reform option offers potentially significant productivity benefits. • Remove some of the prescription currently in the energy laws, rules and regulations in line with the move to a more principles-based regulatory framework. • There is significant value in supporting distribution network businesses to send simpler, more effective price signals to retailers to unlock further value and support retailers to better incentivise customers to participate in virtual power plant offerings, making these programs increasingly scalable. This will help to ensure distribution network capacity is better utilised without unduly penalising customers, particularly those that cannot afford to access CER. • An improved focus (and faster action) on CER interoperability frameworks to enable consumers to easily switch service providers and participate in markets would be highly beneficial and support the recommendations arising from the Wholesale Market Settings Review. • A broad review of the National Energy Consumer Framework to simplify and align obligations across jurisdictions, reduce cost and improve the customer experience. The AEC recommends the above options being tabled for further exploration.
DMO Framework Objectives	
1.1	Refocus DMO Policy Objectives on the most vulnerable: ○ Explicitly prioritise “vulnerable” or truly disengaged customers by narrowing the DMO scope to the “Simple” segment described in the AEC Role of Retailers Project (those with limited market engagement).
1.2	Amend the high-level objectives to address not only price protection and cost recovery, but also: ○ Affordability drivers (e.g., network productivity, CER integration, transition capex). ○ Equity outcomes in a high CER market for low-income and payment vulnerable households.

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Number	Recommendation
1.3	Retain a competition allowance quantum that reflects real customer acquisition and operating costs (particularly for smaller/new entrant retailers), so they can continue to stimulate downward pressure on standing offers.
Keeping the DMO Fit for Purpose	
2.2	Keep the core "price ceiling and common discount baseline" design that has demonstrably reduced headline discounts.
2.3	Ensure the DMO is not set so low that it becomes the cheapest offer, so as not to blunt genuine competitive differentiation.
2.4	Consult on an "exemption pathway" for non-standard products (e.g., CER subscription, dynamic pricing offers), allowing innovators to operate outside rigid volumetric reference rules while preserving core consumer safeguards.
Reference Price Function	
3.1	Encourage the development of tailored, transparent comparison tools (e.g., online calculators that model actual usage patterns or customer CER profiles) to help and encourage customers to see the true value of dynamic and non-volumetric offers.
Aligning pricing with efficient and dynamic market signals	
4.1	Commence the necessary transition from static "efficient cost" models toward frameworks that can accommodate: ○ Locational network charges ○ Time varying wholesale prices ○ Ancillary services and demand response value streams.
4.2	Embed the flexibility to update cost inputs mid period if cost fundamentals shift materially, such as a major capex program or sudden changes in wholesale price drivers.
Leveraging the Competition Allowance:	
5.1	Maintain an allowance component in the DMO that: ○ Reflects smaller retailers' higher marketing and fixed costs. ○ Supports continued new entry, product diversity (like CER orchestration services).
5.2	Complement this allowance with non-price measures to preserve competition, such as: ○ Pathways to easier access to hedging products for small retailers ○ Removing comparison barriers to new service offerings.
DMO/VDO Comparison	
6.1	Consider the comparative study of retail cost stacks between Victoria (VDO) and DMO jurisdictions provided in submissions to understand:

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Number	Recommendation
	○ Network vs wholesale-driven price differences ○ Where any practical effect of headroom exclusion on competitive outcomes can be attributed.
6.2	Use those insights to help calibrate the DMO and VDO differences, rather than assume that Victoria's headroom-free model alone explains lower prices.
Driving innovation	
7.1	Retain an explicit "innovation allowance" (or equivalent) within the DMO to ensure retailers can fund expansion of service offerings, consumer apps, and platform enhancements.
7.2	Lower comparison barriers to encourage competition in service offerings, such as: ○ Demand response programs, CER subscription bundles. ○ EV charging plans, loyalty rewards.
7.3	Monitor non-price innovation metrics as well (e.g., the scope and number of CER integration products) alongside traditional price dispersion measures.
Price Dispersion	
8.1	Track price dispersion to gauge how much is driven by competition versus input cost variance; avoid policy levers that artificially compress or widen spreads.
8.2	Continue to ensure that the cheapest offers remain accessible to those most sensitive to price (e.g., via outreach, hardship programs, proactive offer notifications).

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List of Attachments

Attachment 1	Ernst & Young Report: 2025 Reforms for the Default Market Offer
Attachment 2	AEC Role of Retailer Project
Attachment 3	AEC Responses to Consultation Questions
Attachment 4	List of Recommendations

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Attachment 1:

Ernst & Young Report, 2025 Reforms for the Default Market Offer

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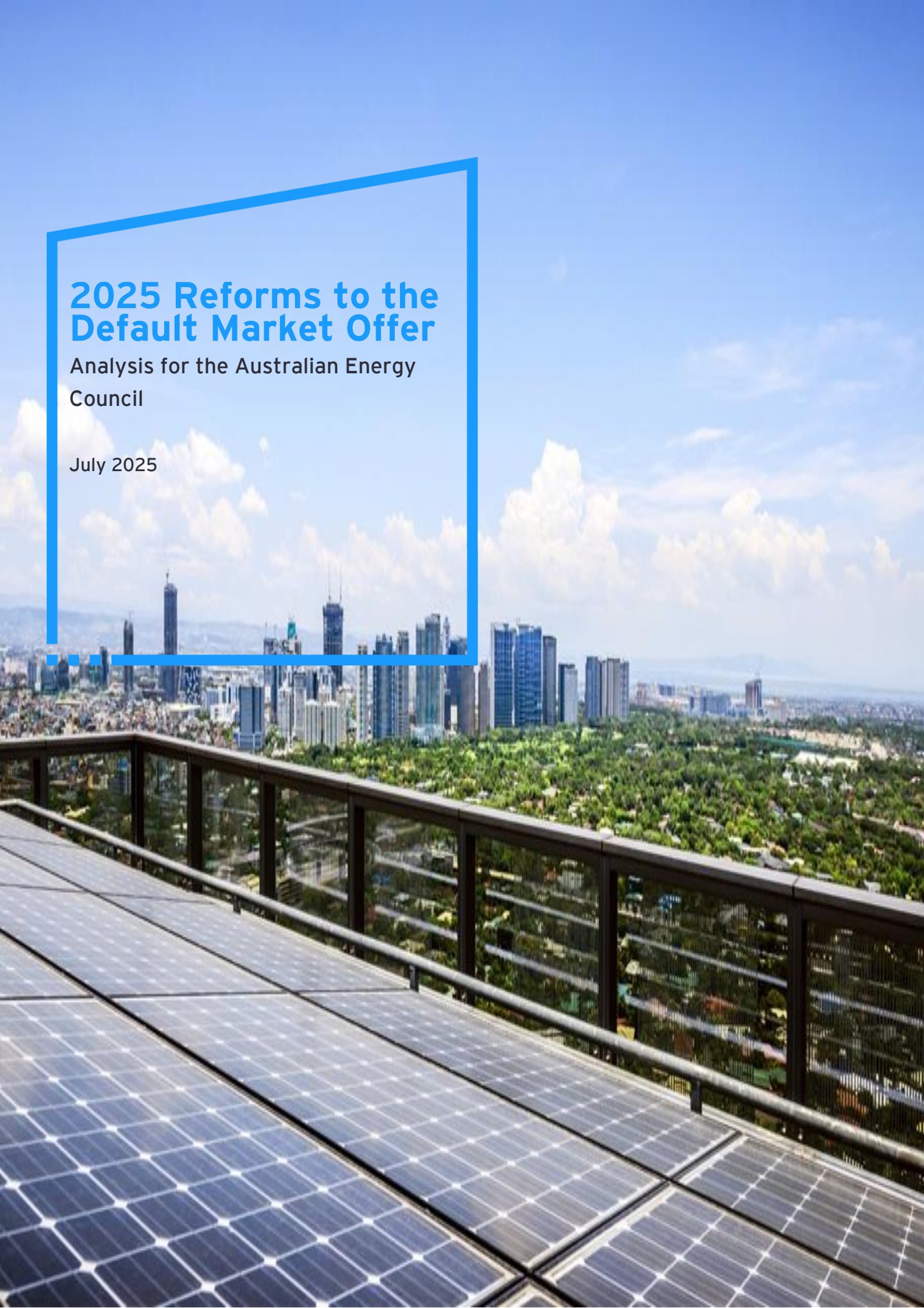

2025 Reforms to the Default Market Offer

Analysis for the Australian Energy Council

July 2025

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Ernst & Young ("**EY**") was engaged on the instructions of the Australian Energy Council Limited ("**Client**") to assess the proposed reforms to the Default Market Offer (DMO) ("**Project**"), in accordance with the engagement agreement dated 4 July 2025 including the General Terms and Conditions ("the **Engagement Agreement**").

The scope of this Project is to provide analysis on the implications of the proposed reforms. The purpose of Project is to inform the Client's submission to the Department of Climate Change, Energy, the Environment and Water's consultation paper on the DMO reforms.

The results of EY's work, including the assumptions and qualifications made, are set out in this paper, dated 22 July 2025 ("**Report**"). You should read the Report in its entirety including any disclaimers and attachments. A reference to the Report includes any part of the Report. No further work has been undertaken by EY since the date of the Report to update it.

Unless otherwise agreed in writing with EY, access to the Report by any party other than the Client (the Recipient) is made only on the following basis and in either accessing the Report or obtaining a copy of the Report the Recipient agrees to the following terms.

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1. Introduction

On 18 June 2025, the Australian Government announced it was reforming the Default Market Offer (DMO). The objectives of the reforms are to ensure customers on a standing offer pay an efficient price that only compensates retailers for the costs incurred in providing an essential service. The reforms propose to remove or minimise the additional costs built into the current DMO framework and methodology to maintain incentives for competition.

The Department of Climate Change, Energy, the Environment and Water (DCCEEW) is now consulting on the proposed reforms. Its consultation paper seeks stakeholder feedback on the following:

1. Whether the objectives of the DMO appropriately balance consumer protections with competitive market outcomes.

2. Whether an efficient pricing framework should be adopted for the DMO.

3. Whether the DMO should be a tariff rather than annual price at a model usage.

EY was engaged to analyse the proposed DMO reforms and their potential implications. This analysis is structured as follows:

- Analysing the difference in approaches to setting regulated retail prices between the DMO and the Victorian Default Offer (VDO), and the varying impacts they can have.

- Examining the drivers of costs making up those prices and the trends impacting them in future.

- Considering the potential consequences of these trends on energy prices and the impact of the reforms, as well as what alternative considerations could be explored to have a meaningful impact on customers who either do not or cannot engage in the energy market.

2. Differences in approaches to setting regulated retail prices

2.1 Differences between the DMO and VDO

2.1.1 What is the DMO

The DMO is a regulated electricity price set annually by the Australian Energy Regulator (AER). It is the maximum price a retailer can charge standing offer customers in New South Wales (NSW), South East Queensland (SEQ) and South Australia (SA). The DMO price also acts as a 'reference price' for all other market offers in each distribution network region, aiding consumers in comparing energy plans across different providers.[1]

The current DMO pricing framework has three key policy objectives:

1. Protect customers from unreasonable prices in the market by reducing unjustifiably high standing offer prices.

2. Allow retailers to recover their efficient costs of providing services, including a reasonable retail margin and costs associated with customer acquisition and retention.

3. Maintain incentives for competition, innovation and investment by retailers, and incentives for customers to engage in the market.[2]

2.1.2 What is the VDO

The most directly comparable approach to the DMO is the VDO. The VDO is set by the Essential Services Commission (ESC) of Victoria. The objectives of the VDO are to provide a simple, trusted and reasonably priced electricity option that safeguards consumers unable or unwilling to engage in the electricity retail market.[3] The VDO sets the maximum prices a retailer can charge for electricity sold to domestic and small business customers in Victoria on a standing offer.

2.1.3 Comparing the DMO and VDO approaches

Table 1 compares the guiding price setting principles of the DMO and VDO. This is followed by Table 2 which provides a comparative overview of each methodology, highlighting similarities and differences.

[1] AER (2025) Default market offer prices 2025-26: Final determination. Available at: https://www.aer.gov.au/system/files/2025-05/AER%20-%20Final%20determination%20-%20Default%20market%20offer%20prices%202025%E2%80%9326%20-%2026%20May%202025_0.pdf

[2] AER (2025) Default market offer prices 2025-26: Final determination. Available at: https://www.aer.gov.au/system/files/2025-05/AER%20-%20Final%20determination%20-%20Default%20market%20offer%20prices%202025%E2%80%9326%20-%2026%20May%202025_0.pdf

[3] ESC (2025) Victorian Default Offer 2025-26 – Final Decision Paper. Available at: https://www.esc.vic.gov.au/sites/default/files/documents/Victorian%20Default%20Offer%202025%E2%80%9326%20Final%20Decision%20Paper.pdf

Table 1: Comparison of DMO and VDO price setting principles[4,5]

Pricing element	DMO principle	VDO principle
Cost recovery	Allow retailers to recover their **efficient** costs of providing services, including a **reasonable** retail margin and costs associated with customer acquisition and retention.	The VDO price determination must be based on the efficient costs of the sale of electricity by a retailer. For this purpose, the ESC must have regard to: ▪ Wholesale electricity costs ▪ Network costs ▪ Environmental costs ▪ Retail operating costs, including **modest** costs of customer acquisition and retention ▪ Retail operating margin ▪ Any other costs, matters or things the ESC considers appropriate or relevant. The VDO Pricing Order does not define 'modest'. In its VDO 2025-26 Final Decision Paper, the ESC notes modest customer acquisition and retention costs are based on the 2013-14 average acquisition cost benchmark from the ACCC retail electricity pricing inquiry report 2018, updated for inflation. The ESC explains it used that benchmark because it was the most robust data available prior to large increases in spending on acquisition costs observed across most jurisdictions.
Headroom	Maintain incentives for competition, innovation and investment by retailers, and incentives for consumers to engage in the market. This is referred to as the competition allowance.	In making a VDO price determination the ESC must not include headroom. This is defined as an allowance that does not reflect efficient costs borne by firms operating in the market.[6]

Accordingly, key differences between the principles of the DMO and VDO are:

- A competition allowance is allowed under the DMO, noting however that the DMO has not included this allowance in the last two years due to sustained cost-of-living pressures.
- Recovery of **reasonable** retail margin and customer acquisition and retention costs under the DMO, versus recovery of **efficient** retail operating margin, and efficient retail operating costs, including **modest** customer acquisition and retention costs.

'Reasonable and 'efficient' are not defined by the regulatory instruments guiding either of the regulated prices. The AER and ESC consider some overlapping data in their methodology to determine retail margin. However, each places a stronger emphasis on different considerations.

In calculating a reasonable retail margin, the DMO methodology includes analysis of:

- Retail margins inferred from 2023-24 EBITDA data reported by retailers.
- Retail margins inferred from the ACCC's customer-weighted average annual prices.

[4] AER (2025) Default market offer prices 2025-26: Final determination. Available at: https://www.aer.gov.au/system/files/2025-05/AER%20-%20Final%20determination%20-%20Default%20market%20offer%20prices%202025%E2%80%9326%20-%2026%20May%202025_0.pdf

[5] ESC (2025) Victorian Default Offer 2025-26 – Final Decision Paper. Available at: https://www.esc.vic.gov.au/sites/default/files/documents/Victorian%20Default%20Offer%202025%E2%80%9326%20Final%20Decision%20Paper.pdf

[6] VDO Pricing Order in Council. Available at: https://www.gazette.vic.gov.au/gazette/Gazettes2019/GG2019S208.pdf

- ACCC analysis of actual margins in its December 2024 report.
- Advertised market offers to infer retail margins.
- Benchmarking regulatory decisions of retail margins in other jurisdictions.

From the range of margins obtained from this analysis, the AER places a greater emphasis on applying a weighted average approach of the inferred retail margins from the retail costs information it collected from 26 retailers representing approximately 99% of the market share in 2023-24.[7] The AER considers it allows a more accurate reflection of the margins faced by a wide range of retailers.

Meanwhile, the VDO uses a regulatory benchmark approach, while also considering other data. This includes the feasible range from the expected returns approach, market offers prices relative to the default offer prices, and retailers' actual margins. In the current VDO, the ESC set a retail margin within the expected returns approach range calculated by Frontier Economics for the ACT's Independent Competition and Regulatory Commission (ICRC).

The table below compares the methodologies used to calculate the DMO and VDO.

Table 2: Methodology comparison[8,9]

Cost stack component	DMO approach	VDO approach
Wholesale costs	Based on forecast load and electricity spot price outcomes, a hypothetical hedging strategy to protect against extreme price volatility. Includes ancillary and prudential costs. This excludes solar exports on the basis the DMO is a price charged for consumption. However, the net system load profile (NSLP) data used to estimate customer load profiles used within the wholesale cost methodology does reflect some customers' solar exports as it cannot be separated out.	Based on the forecast cost of purchasing electricity in the futures market, including a wholesale cost of exports and factoring in a volatility allowance. The VDO excludes solar exports from the customer load profile and uses a load only profile. Network loss factor based on information from the Australian Energy Market Operator (AEMO) is also applied to wholesale electricity costs.
Network costs	Based on updated network flat rate tariffs from the final approved tariffs for 2025-26 for all distributors across DMO regions.	Based on distributors' network tariffs and metering charges approved by the AER.
Environmental costs	Based on a market-based approach to environmental cost forecasting.	Based on retailers' costs of complying with environmental obligations imposed under Commonwealth and Victorian law or regulation. Network loss factor based on information from AEMO is also applied to environmental costs.
Retail costs (including customer retention and acquisition)	Based on a weighted average of retail and other costs (cost to serve and costs to acquire and retain customers). Includes	Based on the customer-weighted average of retailers' actual retail operating costs for domestic and small business customers. These costs include modest customer acquisition and retention costs –

[7] AER (2025) Default market offer prices 2025-26: Final determination. Available at: https://www.aer.gov.au/system/files/2025-05/AER%20-%20Final%20determination%20-%20Default%20market%20offer%20prices%202025%E2%80%9326%20-%2026%20May%202025_0.pdf

[8] AER (2025) Default market offer prices 2025-26: Final determination. Available at: https://www.aer.gov.au/system/files/2025-05/AER%20-%20Final%20determination%20-%20Default%20market%20offer%20prices%202025%E2%80%9326%20-%2026%20May%202025_0.pdf

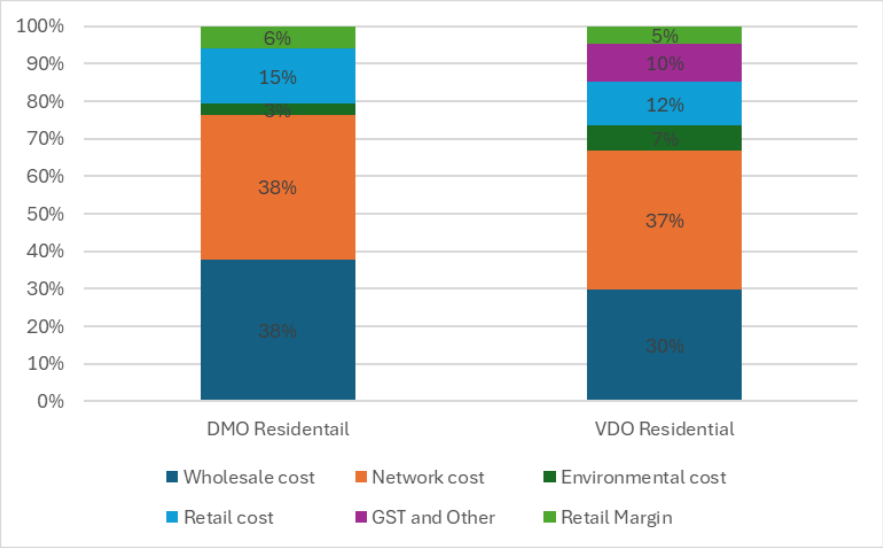
[9] ESC (2025) Victorian Default Offer 2025-26 – Final Decision Paper. Available at: https://www.esc.vic.gov.au/sites/default/files/documents/Victorian%20Default%20Offer%202025%E2%80%9326%20Final%20Decision%20Paper.pdf

Cost stack component	DMO approach	VDO approach
	smart meter costs, and the cost of bad and doubtful debt.	based on the 2013–14 average acquisition cost benchmark updated for inflation.
GST and Other	Other costs are included within other relevant components. For example, AEMO fees are includes within wholesale costs.	Based on costs incurred specific and discrete to obligations and requirements to operate as a retailer, including AEMO fees, ancillary service fees, licence fees and market intervention costs.
Retail margin	Set as a percentage of the DMO price before applying a competition allowance. It is based on analysis of various sources of retail margins in the 2023-24 year.	Based on a retail operating margin benchmark and having regard to market offer prices relative to default offer prices, the expected returns approach and retailers' actual margins. The benchmark considers: ▪ Margins set by other Australian regulators ▪ Market offer prices relative to default offer prices ▪ The expected returns approach ▪ Retailers' observed margins ▪ Submissions.
Competition allowance	Based on calculated values that would allow retailers serving 90% of customers to make a reasonable profit. This is based on the spread of individual retailer costs to serve reported to the AER through formal information requests to retailers. Due to sustained cost-of-living pressure as indicted by the sustained nature of elevated underlying inflation, the last two DMO determinations have not included the competition allowance.	Not allowed.

2.1.4 Comparing the DMO and VDO outcomes

Figure 1 shows a comparison of the average DMO and VDO cost stack components for FY26, noting a different DMO and VDO applies to each distribution network area given network charges are regulated by the AER and are distinct for each network.

Figure 1: Average DMO and VDO cost stack for FY26

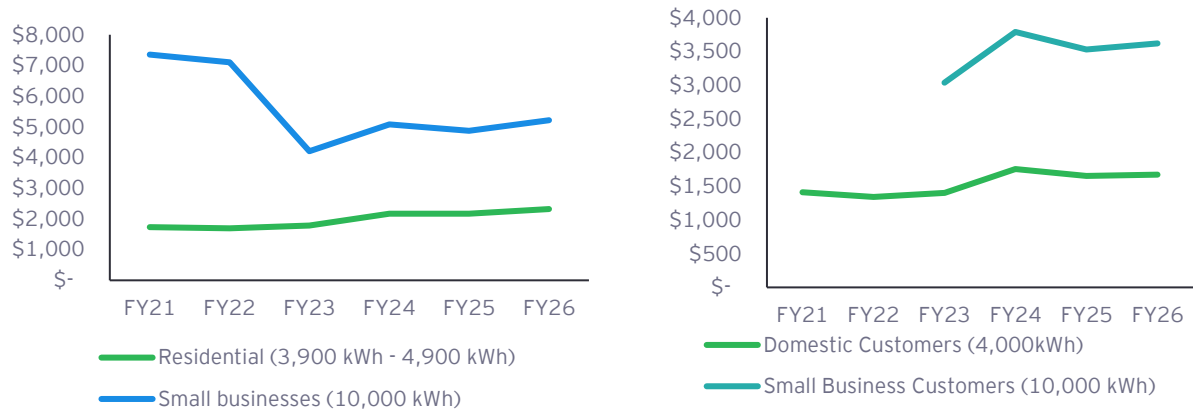


Source: AER (2025) Default market offer prices 2025-26: Final determination, and ESC (2025) Victorian Default Offer 2025-26: Final decision paper.

As shown in the figure above, wholesale and network costs make up the majority of the cost stack for residential customers (76% of the DMO and 67% for the VDO). The retail cost component makes up only 12-15% of the cost stack.

The figure below shows the DMO and VDO price trends over time. The prices in the figure are the average price across the various distribution networks for each customer category shown. Residential customers in the figure reflects customers without controlled load.

Figure 2: Average DMO (left) and VDO (right) price trends



Source: AER DMO price final determinations, and ESC VDO final decisions for each financial year represented in the figure.

Note: VDO prices for small business customers are shown only from FY23 due to changes in reporting by the ESC. Previously it had reported average annual VDO bills for these customers with usage of 20,000 kWh.

The DMO price for 2025-26 for residential customers without controlled load have increased by 1.3% to 9.1% from the previous DMO, depending on the network region.[10] Small business customer prices have increased from 0.8 to 8.5%. For residential customers without controlled load this equates to an average DMO price increase of $154. For small business customers this equates to an average DMO price increase of $340. Meanwhile, the change in the average VDO annual bill component for residential customers has increased by $20 and by $90 for small business customers.[11]

Despite both methodologies being largely similar, particularly while the competition allowance hasn't been included in the DMO, the average residential DMO is $647.00 higher than the VDO for 2025-26. This is most likely due to the average wholesale and network cost being higher across NSW, SEQ and SA than it has been across Victoria.

2.2 Approaches to retail prices in other jurisdictions

The ACT Independent Competition and Regulatory Commission (ICRC), the Queensland Competition Authority (QCA) and Office of the Tasmanian Economic Regulator regulate electricity prices in their respective jurisdictions (the QCA regulates prices for regional Queensland only). A key difference between these approaches and the DMO is that the other frameworks require an 'efficient' price, whereas the DMO is required to be a 'reasonable' price. In these jurisdictions, regulated electricity prices are intended to be efficient prices in their respective markets because there is limited retail electricity competition and thus a lack of competitive tension between retailers.[12]

In the UK, Ofgem sets a price cap for default tariffs (the equivalent to a standing offer) with reference to a stringent efficiency benchmark.[13] The cap is applied universally, which means all customers on the cap pay the same unit rate for energy regardless of circumstances or consumption patterns. The cap is based on the tariff structure that prevailed at the time of its implementation, being a standing charge and flat unit rate.

These alternative approaches are noted here as relevant comparisons, but have not been analysed in detail against the DMO methodology.

[10] AER (2025) Default market offer prices 2025-26: Final determination. Available at: https://www.aer.gov.au/system/files/2025-05/AER%20-%20Final%20determination%20-%20Default%20market%20offer%20prices%202025%E2%80%9326%20-%2026%20May%202025_0.pdf

[11] ESC (2025) Victorian Default Offer 2025-26 – Final Decision Paper. Available at: https://www.esc.vic.gov.au/sites/default/files/documents/Victorian%20Default%20Offer%202025%E2%80%9326%20Final%20Decision%20Paper.pdf

[12] AER (2025) Default market offer prices 2025-26: Final determination. Available at: https://www.aer.gov.au/system/files/2025-05/AER%20-%20Final%20determination%20-%20Default%20market%20offer%20prices%202025%E2%80%9326%20-%2026%20May%202025_0.pdf

[13] Ofgem (2024) Discussion Paper – Future of domestic price protection. Available at: Future of domestic price protection

3. Factors expected to influence trends in each cost stack component

The Australian Energy Market Commission (AEMC) modelled a 10-year outlook for residential electricity prices in the National Electricity Market (NEM).[14] It modelled each component of the cost stack using the generation and demand projections from AEMO's 2024 Integrated System Plan (ISP).

While its modelling projected that all cost components would decrease over the next 10 years, it assumed that the anticipated increase in renewable generation in AEMO's ISP is delivered efficiently and on-time, and also that Consumer Energy Resources (CER) are effectively integrated in a timely and efficient manner.

Recent announcements regarding key transmission projects in AEMO's ISP suggest that the assumptions about timely and efficient connection of new generation are at risk of not being realised, which could in turn delay the downward pressure on energy prices beyond the 10-year horizon. For example, AEMO recently announced a two-year delay in the key VNI West transmission project,[15] and delays and increased cost to other key projects such as Project EnergyConnect. The estimated cost of VNI West has increased by $1.7b, from an estimated $1.6b in 2023 to $3.3b today, and EnergyConnect is expected to cost $1.5b more than originally estimated.[16]

3.1 Wholesale costs

The AEMC projects wholesale prices to fall initially due to a large renewable build out under the ISP Step Change scenario.[17] However, prices are projected to rise toward the end of the 10-year horizon as demand increases and supply conditions tighten. This assumption is being tested as AEMO acknowledged in its 2024 ISP that planned projects are not progressing as expected, due to the time needed for approval processes, investment decision uncertainty, costs pressures, social licence issues, and supply chain and workforce shortages.[18]

The figure below illustrates the trend in generation mix, electricity wholesale prices and price volatility since 2012. The figure shows that as coal generation plants have retired, and the share of renewable generation has grown, there is increasing volatility and an increase in wholesale prices. Wholesale costs are a major driver of retailers' overall costs. Increases in wholesale costs reflect rises in spot prices and contract prices resulting from volatility and take time to be reflected in customer bills.

In the AER's DMO 7 decision, it noted that wholesale costs increased between 1.5%-10% from DMO 6 due to contract prices remaining elevated due to wholesale market volatility.[19] In the AER's 2024

[14] AEMC (2024) residential electricity price trends 2024. Available at: https://www.aemc.gov.au/sites/default/files/2024-11/Price%20Trends%202024%20Final%20Report.pdf

[15] Renew Economy (2025) Key transmission link delayed by two years in new blow to wind and solar projects. Available at: https://reneweconomy.com.au/key-transmission-link-delayed-by-two-years-in-new-blow-to-wind-and-solar-projects/

[16] Australian Financial Review (2025) Key Victorian transmission line hit by two-year delay. Available at: https://www.afr.com/companies/energy/key-victorian-transmission-line-hit-by-two-year-delay-20250701-p5mbr7

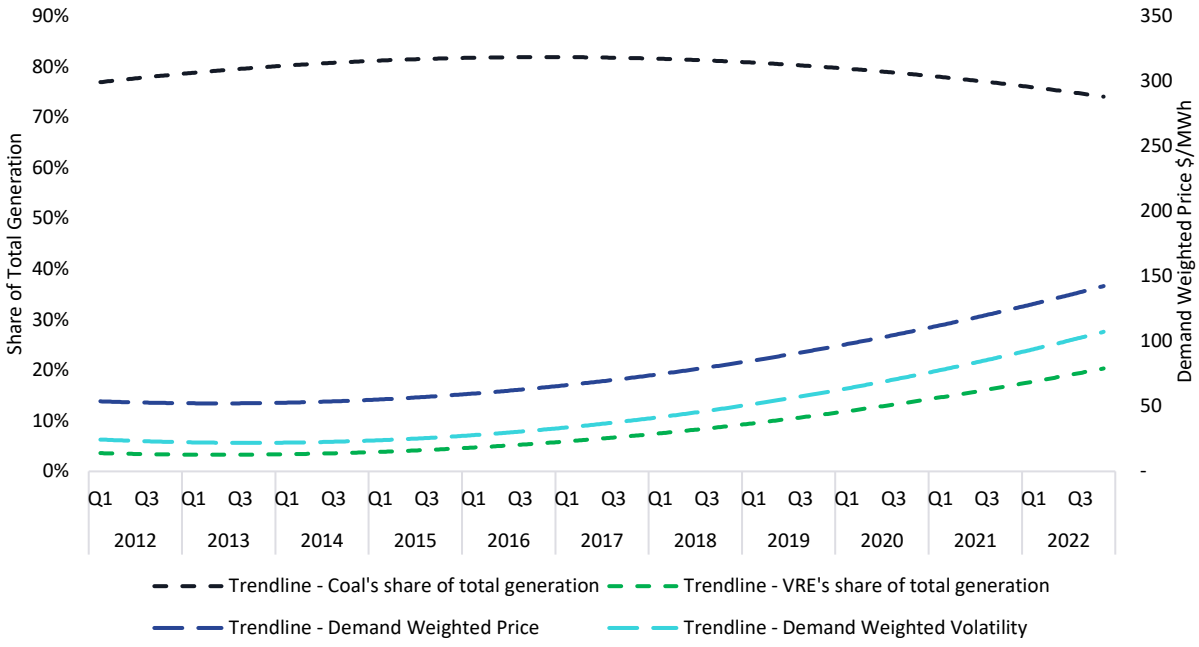
[17] AEMC (2024) residential electricity price trends 2024. Available at: https://www.aemc.gov.au/sites/default/files/2024-11/Price%20Trends%202024%20Final%20Report.pdf

[18] AEMO (2024) 2024 Integrated System Plan. Available at: https://aemo.com.au/-/media/files/major-publications/isp/2024/2024-integrated-system-plan-isp.pdf?la=en

[19] AER (2025) Default market offer prices 2025-26: Final determination. Available at: https://www.aer.gov.au/system/files/2025-05/AER%20-%20Final%20determination%20-%20Default%20market%20offer%20prices%202025%E2%80%9326%20-%2026%20May%202025_0.pdf

Wholesale Electricity Market Performance Report, it noted that the risk of volatility in the wholesale market remains, given the ongoing lumpy nature of thermal generation exits.[20]

Figure 3: Historic price and generation in the NEM



Source: EY analysis of NEM market data.

3.2 Network costs

The AEMC projects network prices to fall by 11% over the next 10 years, despite the higher levels of network investment that will need to be recovered from customers.[21] The AEMC conducted sensitivity analysis that projected that sub-optimal CER orchestration would have a large impact on network prices. The AEMC noted that if demand from increased electrification, electric vehicles and other CER is not well coordinated, electricity prices could increase for all households. Effective coordination of CER would enable a reduction in network investment that would otherwise be needed to manage higher peak demand and lower minimum demand that can arise as more CER is connected to the network. Overall, lower network investment would lower electricity costs for all consumers, both with and without CER, including DMO customers. However, while a number of successful trials are proving how orchestration might work in practice, significant challenges remain in applying orchestration more broadly across all CER customers. EY research observed many customers do not trust third parties controlling their CER devices, even if it saves them money.[22]Customers would be willing to take action to manage their energy use but they want notifications and personal control. Overall, this indicates industry faces challenges to build customers' trust to a level that would achieve optimal CER orchestration to lower overall system costs.

[20] AER Wholesale Electricity Market Report 2024. Available at: Wholesale electricity market performance report - December 2024.pdf

[21] AEMC (2024) residential electricity price trends 2024. Available at: https://www.aemc.gov.au/sites/default/files/2024-11/Price%20Trends%202024%20Final%20Report.pdf

[22] EY P&U CXT Research 2023 (Australian respondents)

The cost of building new Renewable Energy Zones (REZs) is also starting to flow through to customer bills and will continue to do so over the medium term. As noted earlier, transmission costs have been increasing.

3.3 Environmental costs

The AEMC's outlook projects renewable and energy efficiency scheme costs to fall over the 10-year horizon, as a several schemes as expected to sunset in 2030.[23]

3.4 Retail costs

In the AER's DMO 7 decision, retail costs increased by between 8.3% and 15%, and at a faster pace than other cost components. It noted that this increase is due to greater bad and doubtful debts and the cost of smart meter rollouts, with some retailers also increasing their spending on acquiring and retaining customers.[24]

The AEMC's outlook projects retail costs to be flat over the 10-year horizon.[25] The AEMC also projects metering costs, which incorporate the roll-out of smart meters by 2030, will be stable over the horizon. Though the modelling projects metering costs to increase slightly initially, the costs stabilise as legacy accumulation meters are replaced.

Bad and doubtful debt trends are difficult to predict and are impacted by a range of factors that relate to the broader economic environment, but it is likely that these increased costs will remain while Australians continue to experience cost of living pressures.

3.5 Retail margins

The ACCC December 2024 report found that retail margins increased overall in the 2023-24 financial year but varied greatly among retailers.[26] The ACCC reported that retail margins increased from 2% to 6% of customer bills during this period across all regions. However, the ACCC notes high overall margin results were driven by a subset of retailers, with outliers being a significant driver in some regions. It also notes that while this represents a significant increase, margins have been relatively low in recent years. The ACCC provides a possible explanation for the increase in retail margins could have been driven by unique circumstances in the 2023-24 financial year. The ACCC explains that higher overall costs caused most retailers to increase their prices from July 2023. The ACCC notes some retailers were able to avoid some of these cost increases and this could have allowed those retailers to set competitive prices while earning higher margins. The ACCC observed its data shows retailers with lower wholesale costs tended to have higher margins. Meanwhile, the ACCC also notes that several retailers in its sample reported losses in the past few years.

The ACCC notes the combination of factors affecting the 2023-24 margin outcomes and relatively lower margins in recent years means it is uncertain if increased margins will continue in the future. Until now, the ACCC has observed a declining trend in retail margins since a peak in 2016-27. While it is unclear the direction retail margins will take, trends in wholesale electricity prices could impact retail margins over the next few years given the influence it has on costs.

[23] AEMC (2024) residential electricity price trends 2024. Available at: https://www.aemc.gov.au/sites/default/files/2024-11/Price%20Trends%202024%20Final%20Report.pdf

[24] AER (2024) Default Market Offer Prices, 2025-26, Final Determination. Available at: Default market offer prices 2025-26: Final determination

[25] AEMC (2024) residential electricity price trends 2024. Available at: https://www.aemc.gov.au/sites/default/files/2024-11/Price%20Trends%202024%20Final%20Report.pdf

[26] ACCC (2024) Inquiry into the National Electricity Market – December 2024. Available at: https://www.accc.gov.au/system/files/accc-national-electricity-market-december-2024-report.pdf

3.6 Likely outcomes for consumers from these trends

The reduced energy prices projected by the AEMC are dependent on an orderly and timely energy transition. Recent announcements regarding cost increases and delays in essential transmission required to connect new generation assets to the grid suggest that this may not be the case.

If delays in building the required transmission and generation assets persist, it is likely to lead to increased network and wholesale costs, which are the main components of energy bills.

The effective and timely orchestration of CER is also required to put downward pressure on wholesale and network costs. Trials are underway and network businesses are investing in measures to enable this. However, the successful deployment of widespread CER orchestration is likely to take several years to realise.

Retail costs are a relatively small component of energy bills. Some of the current trends impacting retail costs are difficult to predict and cannot be controlled by a regulated price, such as bad and doubtful debts, while others can be more easily controlled either by retailers or through a regulated price, such as the cost of smart meter rollouts, margins and customer acquisition costs. Changes to the factors influencing retail costs that can be controlled may lead to a reduction in bills, although it is likely to be comparatively smaller impact given the size of this component in the cost stack.

4. Examining the potential consequences of the reforms

4.1 The potential consequences of removing a competition allowance

4.1.1 Modest impact due to the nature of the cost stack

The DMO allows a competition allowance based on the principle that retailers should be able to make a reasonable profit, although it has not been included in the two most recent DMO decisions.[27] Even though it was not included in this year's DMO, the AER nonetheless calculated a competition allowance that would allow retailers serving 90% of customers to make a reasonable profit. This was calculated at $22.61 for residential customers, and $26.19 for small businesses customers, excluding GST.[28] While permanently excluding the competition allowance would reduce the overall DMO prices, it is unlikely to have a material impact because it is a small component of the bill compared with wholesale and network costs.

4.1.2 Potential impacts on choice

In its decision to exclude the competition allowance, the AER stated it did not consider doing so would restrict competition because DMO prices include a retail margin, and thus still allows retailers to compete.[29] However, individual retailers incur different operating costs to the benchmarks applied in the calculation of the DMO and VDO.

Further, smaller retailers have an incentive to acquire the disengaged customers of the larger incumbent retailers. For competition to flourish and provide choice and downward pressure on energy bills, smaller retailers need to be able to incur costs to acquire customers and make a reasonable profit. If the margin is set too low and there is no allowance for competition, it could make the market less attractive for new market entrants and lead to existing retailers existing the market, leading to less choice and an absence of competitive tension to put downward pressure on prices. Additionally, it could also lead to reduced incentives for retailers to develop innovative products and services, including those that would encourage greater level of orchestration of customers' CER.

If the incentive to compete is reduced, it will lead to less choice and therefore less incentive for customers to engage in the market.

4.2 Case study

Ofgem case study

On 19 July 2018, the *Domestic Gas and Electricity (Tariff Cap) Act 2018* came into force in the UK. This legislation required Ofgem to design and implement a temporary cap on a default tariffs.[30] Default tariffs are the equivalent of the standing offer.

[27] AER (2025) Default market offer prices 2025-26: Final determination. Available at: https://www.aer.gov.au/system/files/2025-05/AER%20-%20Final%20determination%20-%20Default%20market%20offer%20prices%202025%E2%80%9326%20-%2026%20May%202025_0.pdf

[28] AER (2025) Default market offer prices 2025-26: Final determination. Available at: https://www.aer.gov.au/system/files/2025-05/AER%20-%20Final%20determination%20-%20Default%20market%20offer%20prices%202025%E2%80%9326%20-%2026%20May%202025_0.pdf

[29] AER (2025) Default market offer prices 2025-26: Final determination. Available at: https://www.aer.gov.au/system/files/2025-05/AER%20-%20Final%20determination%20-%20Default%20market%20offer%20prices%202025%E2%80%9326%20-%2026%20May%202025_0.pdf

[30] Ofgem (2018) Decision – Default tariff cap – Overview document. Available at: Default Tariff Cap - Overview Document

The policy was introduced following concerns that households were paying excessive prices for electricity, which was attributed to suppliers passing through inefficient high operating costs, and a 'loyalty penalty'.[31]

While the cap was initially introduced as a temporary intervention, it was eventually implemented permanently based on Ofgem's assessment that without some form of price protection, price exploitation of inactive customer would likely return.

In its discussion paper on the future of price protection, Ofgem noted the cap appeared effective immediately following its introduction because default tariff customers saved on their bills and suppliers invested to improve efficiency. However, Ofgem admits the last few years have demonstrated some limitations of the cap. In response, Ofgem made changes to the cap to make it more responsive to market conditions, but it acknowledges issues remain.[32]

Ofgem outlines the key challenges of the current cap as:

- Additional costs and risks as a side effect of the cap design, including supplier failure during extreme market volatility. To mitigate risks, retailers are required to hold more capital, but this in turn increases costs for consumers.

- Impacts on competition, innovation and service levels over time as a result of the existence and design of the cap. Ofgem notes it is important to consider adverse effects on consumers if the cap reduces incentives on suppliers to offer more competitive prices or to offer better services through improved efficiency and innovation. Ofgem considers the overall effect of the cap on competition will depend on the relative importance to customers of the price of energy versus non-price factors such as more innovative tariffs and service levels. It notes that while the cap may reduce competition in the short-term, the medium-term effect on innovation-led competition is less clear.

- The growing challenge of applying the cap to an increasingly diverse market, especially when considering growing bad debt levels. Ofgem notes a stringent one-size-fits-all cap may create challenges for some suppliers that have higher cost to serve customers than other suppliers.[33]

In May 2025, Ofgem restructured how it calculates operating cost and debt allowances. This includes benchmarking supplier costs, reallocating costs across customer groups, and updating the methodology for each cost component to ensure customers pay a fair price for their energy that reflects the efficient underlying cost to supply that energy.[34]

Ofgem is also exploring alternative tariff models to create a more flexible, customer-responsive energy market and reduce reliance on a static price cap.[35] To address affordability, which Ofgem recognises cannot be tackled by the price cap, it is exploring support mechanisms for vulnerable customers. It notes that a universal price cap does not adequately protect vulnerable customers as rising electricity supply costs and flat-rate protections disproportionately impact low-income and low-usage households.[36]

The Ofgem experience demonstrates that there is no easy solution, and illustrates the challenges associated with developing an appropriate approach to retail price caps and the unintended consequences that can result.

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[31] Ofgem (2024) Discussion Paper – Future of domestic price protection. Available at: Future of domestic price protection

[32] Ofgem (2024) Discussion Paper – Future of domestic price protection. Available at: Future of domestic price protection

[33] Ofgem (2024) Discussion Paper – Future of domestic price protection. Available at: Future of domestic price protection

[34] Ofgem (2025) Decision - Energy price cap operating cost and debt allowances decision: overview. Available at: Energy price cap operating cost and debt allowances decision: overview

[35] Ofgem (2024) Discussion Paper – Future of domestic price protection. Available at: Future of domestic price protection

[36] Ofgem (2024) Discussion Paper – Future of domestic price protection. Available at: Future of domestic price protection

4.3 Other considerations

The reforms to the DMO seek to ensure that customers who do not or cannot engage in the market are protected from unreasonably high prices. An element of this challenge is addressing the issue of the 'loyalty penalty'. A loyalty penalty refers to the extra fees or charges that long term customers may pay for the same product or service compared to new customers. It is the result of practices by companies incentivising and rewarding new customers with discounted prices or better offers, while covering their costs by charging loyal customers more.

The energy retail industry is not the only industry where loyalty penalties are observed. Other industries where this has been observed include telecommunications, insurance, banking and financial services. While the market structures of these industries are different, the effect of the loyalty tax is the same for customers. For example, in the financial services industry, a lender may offer a discounted rate for new customers signing up for a mortgage, while existing customers continue being charged a higher rate for the same type of loan.

Concerns in both the financial services sector and the electricity sector have been closely scrutinised by the ACCC and the Productivity Commission.[37] While the two industries have fundamental differences in market structures, the two commissions identified common concerns and made common proposals to address those concerns. In terms of pricing and a loyalty tax, both commissions advocated for the Consumer Data Right as a way to improve competitive outcomes, including encouraging switching and helping consumers to avoid the loyalty tax by making markets more transparent. Similarly, both inquiries emphasised the need to reduce retail prices and improve the ways offers are marketed to allow customers to more easily compare offers.[38]

In the UK, the Financial Conduct Authority (FCA), which regulates financial services firms and markets in the UK, implemented rules prohibiting renewal quotes for home and motor insurance consumers from being more expensive than they would be for new customers. Industry analysis indicates the reforms resulted in insurance firms re-strategising their pricing practices to attract new customers but the long-term benefits for customers remained uncertain:[39]

- Some industry research suggested that one of the unintended consequences was for firms to 'brand stack'.[40] This is a practice where the firm strips back a previously comprehensive product to varying degrees at increasingly cheaper prices (i.e. the less comprehensive, the cheaper the product). This risk may not apply to the NEM to the full extent as has been observed in the UK insurance industry, given the National Energy Retail Rules (NERR) and Electricity Retail Code of Practice (ERCP) set out minimum requirements for both standing and market offers. Meanwhile, other analysis indicates that the rules to end the loyalty penalty and make policy costs fairer for customers has led to higher prices across the board.[41]

- The FCA has since announced an evaluation of the impact of its pricing reforms to assess unintended consequences.

[37] Allens (2018), Competition in electricity and financial services markets – common issues, common solutions? Available at: Competition in electricity and financial services markets - common issues, commo

[38] Allens (2018), Competition in electricity and financial services markets – common issues, common solutions? Available at: Competition in electricity and financial services markets - common issues, commo

[39] Clifford Chance (2024) FCA indicated response to rising retail market insurance premiums. Available at: https://www.cliffordchance.com/insights/resources/blogs/insurance-insights/2024/02/fca-indicates-response-to-rising-retail-market-insurance-premiums.html

[40] Insurance Times (2024): Opinion: Has brand stacking replaced the loyalty penalty? Available at https://www.insurancetimes.co.uk/analysis/opinion-has-brand-stacking-replaced-the-loyalty-penalty/1452359.article#:~:text=The%20motor%20and%20home%20markets,policy%20statement%20in%20May%202021.

[41] The Times (2025) The legacy of the insurance crackdown: now we are all paying more. Available at: https://www.thetimes.com/business-money/money/article/insurance-crackdown-now-we-are-all-paying-more-7xztt8lpn#:~:text=The%20regulator's%20move%20to%20end,the%20board%2C%20finds%20George%20Nixon&text=It%20has%20been%20three,what%20you%20need%20to%20know.

A study by the University of New South Wales (UNSW) cautioned that well-intentioned policies to ban loyalty penalty practices (e.g. by limiting the price differential between new and existing customer markets) could have unintended consequences that could potentially cause more harm to customers than good.[42] Specifically, the study notes if there are limits to the price difference among the two markets (existing and new customers), companies may end up not undercutting each other at all and thus resulting in prices higher than they otherwise could be. However, the study also notes that if carefully designed, policies could achieve their intended outcome to address loyalty penalty practices. The report explains that in a highly competitive market, limiting loyalty taxes could alleviate cutthroat competition among companies, and thereby possibly resulting in higher profits for firms. The study notes this could also be a win for customers as it can save customers from constant switching without penalising unengaged customers.

The UK has sought to address the same loyalty penalty issue in the retail electricity market. While Ofgem considers its price cap has played a role in protecting customers from the loyalty penalty, it has also introduced additional measures to address it. Ofgem has retained a ban preventing retailers from offering lower prices exclusively to new customers.[43] This is known as the ban on acquisition-only tariffs (BAT). The BAT was introduced as a temporary measure in 2022 to protect customers during the wholesale price crisis when prices were extremely high and volatile. Following consultation on a proposal to end the ban, it decided to extend the ban until at least 31 March 2026. In the meantime, it will consider whether it should remain a permanent policy, and if so, how it could be improved. In its decision, Ofgem noted it was persuaded of the qualitative benefits of retaining the BAT, while acknowledging its removal would also bring benefits for active switchers and competition.

These examples illustrate the complexity of the challenge and the scope and scale of unintended consequences that can arise when addressing loyalty penalties.

4.4 Conclusion

There are no easy options to reduce energy prices in the context of the energy transition. Removing the competition allowance is likely to reduce DMO prices, but it is not likely to be a significant reduction, given the size of the retail component of the energy bill. In order to make a significant impact on energy bills over the course of the energy transition, broader reforms that address wholesale and network costs, that enable an orderly, timely and cost-effective transition are required. Such reforms are being actively considered and pursued by governments. However, they are complex and will take time to develop and implement.

In addition, the way in which energy prices are considered and compared over time is also likely to require a change in approach. This is because as transport is electrified and customers transition away from gas to electric alternatives, a customer's energy bill will be a combination of their electricity, gas and fuel bills today. As such, the way in which price increases and customer protections are viewed needs to be considered in this evolving context.

[42] UNSW (2024) How banning loyalty penalties can help – or hurt – consumers. Available at: How banning loyalty penalties can help – or hurt – consumers - UNSW BusinessThink

[43] Ofgem (2024) Decision: Future of the Ban on Acquisition-only Tariffs (BAT) beyond March 2025. Available at: https://www.ofgem.gov.uk/sites/default/files/2024-11/Decision_Future_of_the_Ban_on_Acquisition_only_Tariffs_after_March_2025.pdf

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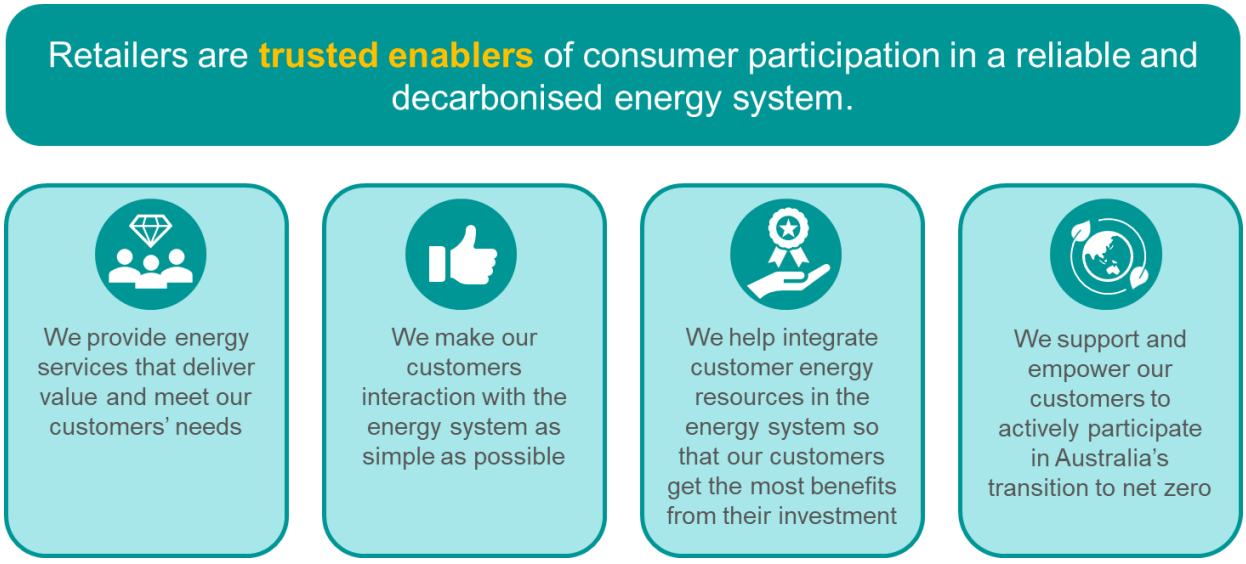
Attachment 2:

AEC Role of Retailer Project

Retailers as enablers of customer participation in the future energy system

The future electricity system is likely to be more dynamic than the current system. The future energy market may offer more choices and different types of interactions with the electricity system for some consumers, but it may also present more complexity and be more difficult to navigate for others. We urge DCCEEW to develop recommendations that consider the needs of all customers, regardless of whether they have CER or not, or whether they have more or less capacity or willingness to engage with future energy markets.

The AEC and its members consider that retailers have an important role as trusted enablers of customer participation in a future electricity system that is reliable and decarbonised. The diagram below is a future retailer vision that we have developed with our retail members:



Needs and values of the customer

As the energy market evolves, customers will increasingly want flexibility, control and community-driven value, as shown by the diagram below. It is important that the customer protection framework enables these customer outcomes.

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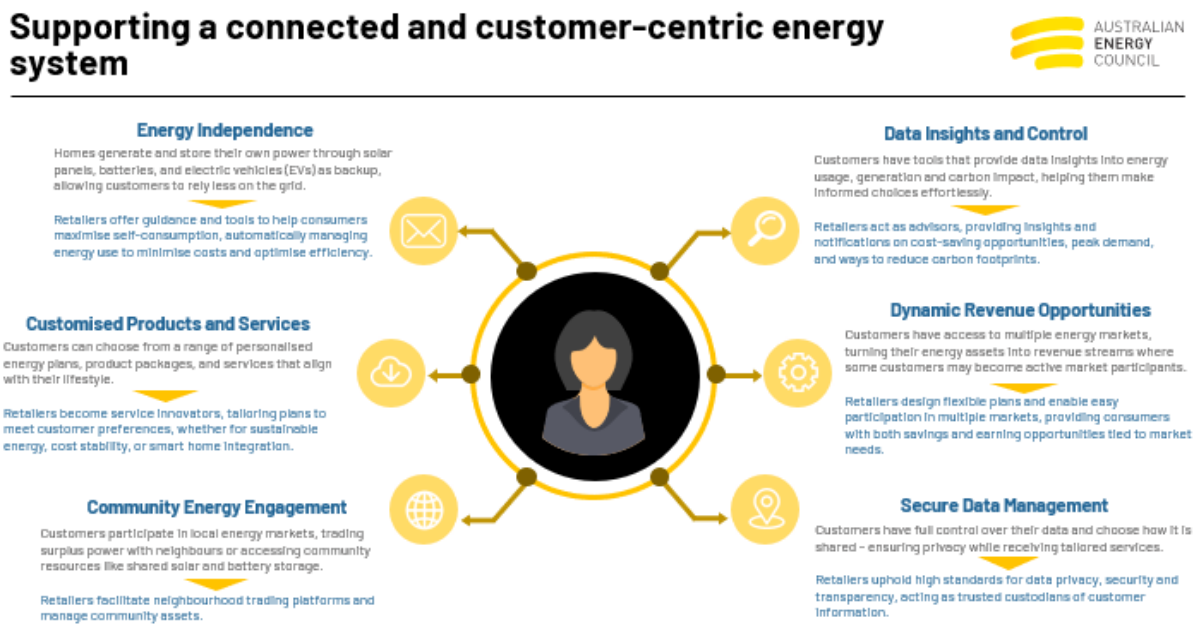

The AEC has identified shared needs and values amongst all customers for:

- Simplicity
- Reliability and certainty
- Affordability
- Comfort and convenience
- Choice and agency
- Customer protections and security
- Fairness and equity
- Environmental sustainability.

The AEC also notes that opportunities for customers to be rewarded as they increasingly engage include:

- Dynamic network pricing
- New value streams and auxiliary markets
- Emerging CER technologies
- Electric vehicles and vehicle-to-grid capabilities
- Energy market policy reforms
- Load flex and CER orchestration
- Smart and digital management technologies
- Set and forget devices.

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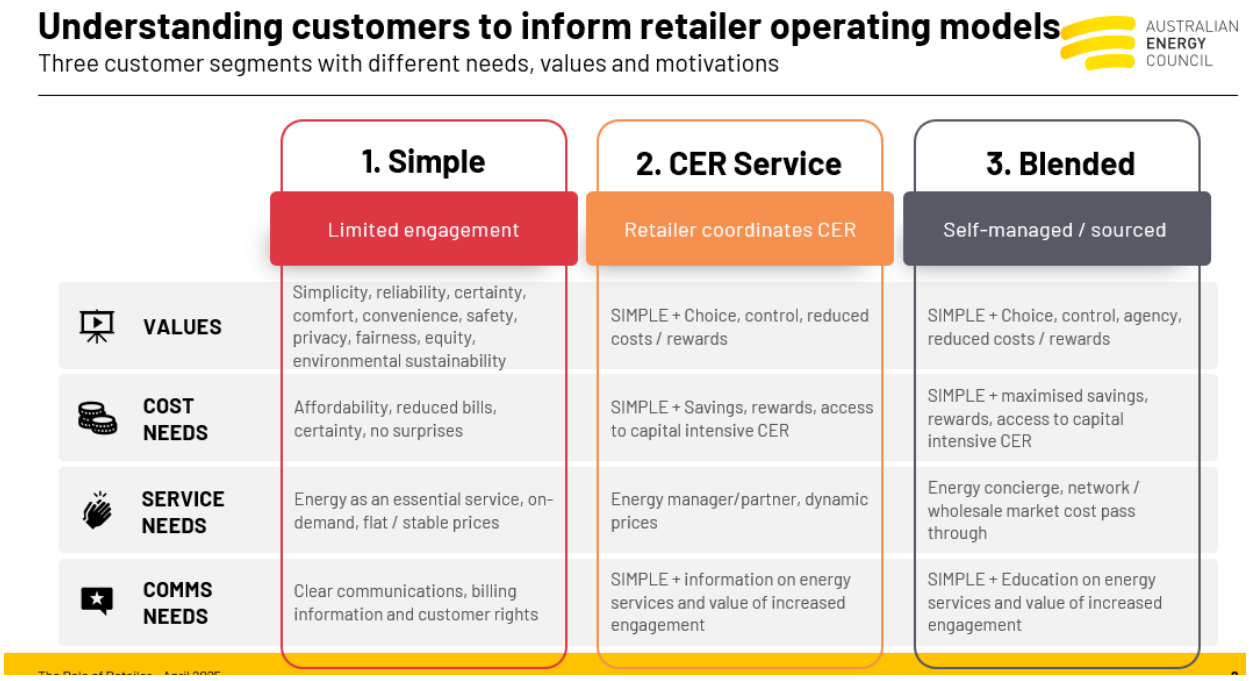
The AEC has developed a customer segmentation framework that enables consideration of the different types of customers. The segmentation framework is an engagement spectrum, with customers moving to increasing engagement as they move from 1 to 3 in the framework:



The percentage of customers in each segment is:

- Simple – unengaged 25% , green conscious renters 19% (barriers to investing in assets), comfort seekers 17% (61% total)
- CER-service – cost conscious baby boomers 25%
- Blended - green tech adopters 14%[13]

As the customer framework evolves, it is important to ensure that all types of customers are protected, not just the more engaged customers. The 61% of customers who are at the simple end of the engagement spectrum form the largest segment, and it is vital to consider consumer protections that will support their inclinations towards more transactional relationships and barriers to investing in technology and assets.

The diagram below shows the increasingly complex nature of the energy market and participant relationships. Customers are faced with potentially negative experiences and consumer detriment if this complexity is not managed well. Retailers believe that it is important for retailers to remain the primary

[13] Connecting the new energy customer | Deloitte Australia | Energy, Resources & Industries

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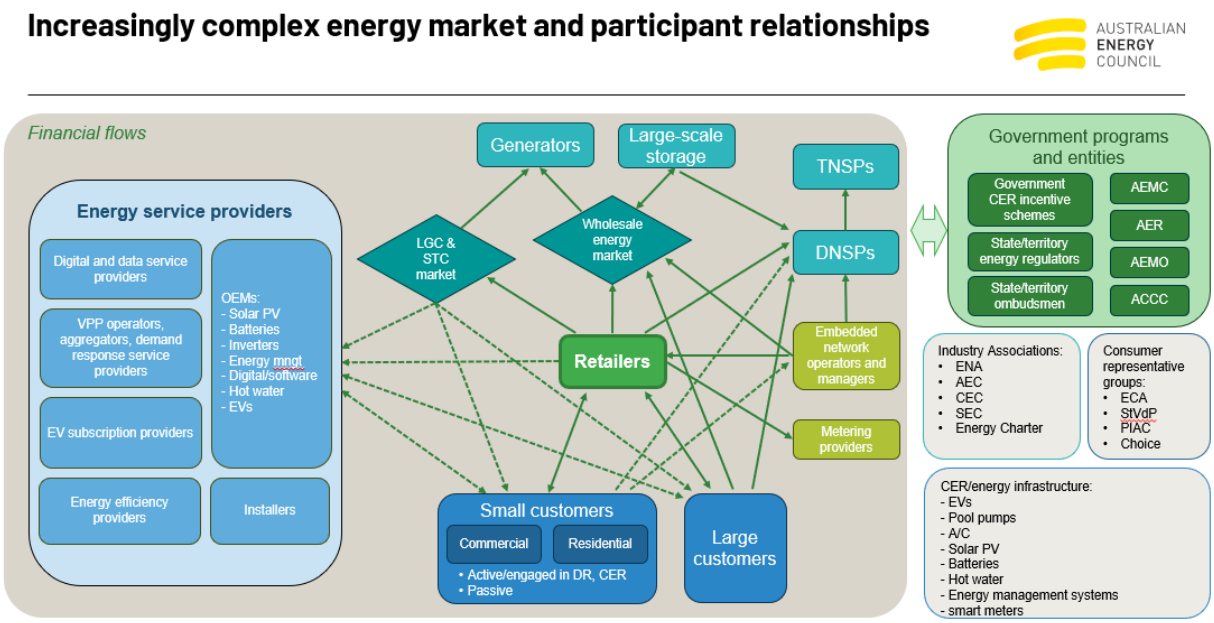
customer agent so that retailers can manage this complexity for customers as a default setting, but where the customer chooses to have more engagement, they are still able to do so.



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Appendix 3:

Responses to specific consultation questions

1. DMO Framework Objectives

Q1: How can the DMO framework policy objectives be amended to adopt greater emphasis on protections for disengaged customers in competitive retail markets?

Response:

The DMO framework Policy Objectives

The current objectives include important aims—price protection, cost recovery, and competition. However, these create inherent tensions. That a customer is on a standing offer does not by definition mean they are disengaged (as the consultation paper claims). And these customers do benefit from competition; from the pressure it puts on service delivery and the cost to serve, as well as the upstream benefits discussed in other questions below.

Smaller retailers, in particular, play a critical role in stimulating competitive pressure by targeting disengaged customers of larger incumbent providers. For these participants to compete effectively, they must be able to recover the costs associated with customer acquisition and earn a reasonable return.

Prioritising the protection of vulnerable consumers requires a clearer emphasis on addressing the matters affecting affordability (the wall of capex, the transition, and CER integration). These are drivers. As Bruce Mountain described, "we can't solve social issues by tinkering with price controls."[14] Amending the objectives to explicitly prioritise the protection of vulnerable customers and to address the real contributors to affordability, with improvements to distribution network productivity, would be a start.

In its recent decisions to exclude the competition allowance, the AER noted that doing so would not undermine competitive outcomes, as the DMO still includes a retail margin that enables retailers to recover costs and remain commercially viable. However, it is important to recognise that individual retailers face differing cost structures, which may not align with the benchmark assumptions underpinning the DMO and VDO methodologies. For example, smaller new entrant retailers are particularly vulnerable to higher wholesale costs. We observed this during the energy crisis in 2022, when there was an unprecedented number of Retailer of Last Resort events.

[14] Mountain, B. (2025) ABC 7.30 Report interview, 30 June 2025.

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Thus, if the regulated margin is set too narrowly, and no allowance is made for competitive dynamics, the market may become less conducive to new entry and innovation. This could result in reduced consumer choice, diminished competitive tension, and lower investment in new retail offerings and services such as those that support the orchestration of customer energy resources (CER). Such outcomes would risk weakening both the efficiency and equity objectives of the retail energy market.

To keep it simple, the scope of the DMO should be narrowed to focus on the segment/s of customers that have the most difficulty engaging in the market. In the AEC's *Future Role of Retailer Project* (Attachment 2), we framed our discussion around three categories of customers, each with their own needs and driven by different motivators.

Simple	CER Service	Blended
Limited market engagement	Retailer coordinates CER	Self-managed & sourced CER

The DMO should be targeted to those in the 'Simple' segment that relies on the DMO for price comparison and protection. A volumetric tariff reference price provides little value for customers in the CER Service or Blended customer segments given these customers are engaging in CER or other technologies that make comparisons with a volumetric reference price redundant.

Retailers will be trying to interest customers in migrating from limited market engagement into a retailer-coordinated CER service. The incentive is both share of market as CER expands and becomes an increasingly valuable resource and share of wallet as customer interest in value-add grows. This can include product value adds beyond CER, such as Netflix or other loyalty incentives.

Reference pricing in the CER service and Blended categories could stifle innovation in technology-based products and services, as comparing these types of technology-based or value-added offerings to a volumetric reference price based on a standard consumption profile makes more innovative offers harder to develop, and to communicate to customers in a way that is not confusing.

We would encourage DCCEEW to further analyse the reasons for differences in regulated retail pricing outcomes between Victoria and the DMO jurisdictions, and between the DMO jurisdictions. We anticipate that this will show that such differences are more a reflection of differences in the state of generation across jurisdictions (e.g., brown vs. black coal, solar penetration, large-scale batteries), wholesale markets outcomes and network activities. The differences between the DMO jurisdictions also

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need examination in context. For example, in DMO 7, the increase in NSW for residential consumers without controlled load ranged from 8.5% to 9.1% but was 3.7% in Southeast Queensland for the same customer classes and only 3.2% in South Australia. Yet all the while, the method employed to calculate the retail cost component and the margin was the same. Retail is not the contributing lever that needs adjusting.

Competition and the disengaged customer

Competition can play a powerful role in eroding the "loyalty penalty", those higher prices that incumbent firms tend to reserve for their most captive, least price-sensitive or engaged customers. At its core, competition disciplines incumbents by forcing them to treat all customers (including their long-standing ones) as potential leavers. That is the disengaged customers' best protection.

In energy, there are close to, if not completely zero, switching costs. There are clear comparable offers and there are many price comparators and services a customer can easily use. There are obligations to pro-actively offer best deals, along with active nudges to encourage the customer to consider them. These are all tools to remove barriers to exit, highlight the cost to the customer of loyalty, and ensure challengers emerge. Every customer is turned into a potential churn risk. What more can be done?

You can regulate for an efficient price as proposed. But when you do that, you take away the very market that you need to ensure both the development of lower cost offers, and the effective integration and optimisation of CER. And for that, you need dynamic pricing and time-varying prices linked to real costs: to locational network charges, wholesale energy prices, and ancillary services markets. And you need flexible market products for demand-response, for frequency response, for network support services, and wholesale market arbitrage so CER can be dispatched alongside traditional generators.

You need a fit-for-purpose exemption framework for retailers offering products that fall outside the standard DMO/VDO constructs. For example, CER or subscription-based offers may be subject to rigid price comparison and contract disclosure obligations that were not designed for these models. An automatic and established exemption framework could allow for regulatory flexibility while maintaining core protections.

And mostly, you need scale. You need to engage these disengaged customers, not just to lower the activation threshold for truly disengaged customers. You need to turn passive bill-payers into informed, proactive consumers. What has been done to date in retail competition has helped turn every retail

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customer into a potential churn risk. The focus for the transformation should be to supercharge that, not to kill it off.

Recommended approaches:

- Refocus DMO Policy Objectives on the most vulnerable:
    - Explicitly prioritise "vulnerable" or truly disengaged customers by narrowing the DMO scope to the "Simple" segment described in the AEC Role of Retailers Project (those with limited market engagement).
- Amend the high-level objectives to address not only price protection and cost recovery, but also:
    - Affordability drivers (e.g., network productivity, CER integration, transition capex).
    - Equity outcomes in a high CER market for low-income and payment vulnerable households.
- Retain a competition allowance quantum that reflects real customer acquisition and operating costs (particularly for smaller/new-entrant retailers), so they can continue to stimulate downward pressure on standing offers.

2. Fit-for-Purpose Test

Q2: Does the DMO framework remain fit-for-purpose, noting the rationale for its introduction in 2019 was to address specific concerns regarding the discounting behaviour by retailers identified in the ACCC's REPI report?

Response:

The ACCC recommended that policymakers should devise measures to limit the number and size of legacy conditional discounts and to improve transparency around discount eligibility and achievement conditions. Their findings showed that the discounts were often more promotional window dressing than genuine price relief, with some retailers setting their headline rates high, then offering a discount to bring them back down to or just above the same level as the then uncapped default offers. This made meaningful comparison and true cost savings extremely difficult for consumers.

The DMO has the following features:

- It places an absolute ceiling on what any retailer can charge on a standing (default) contract, ensuring no customer who remains disengaged can face an unbounded tariff.
- It provides a common reference point for tariffs, such that all conditional discounts advertised by retailers must be calculated off the same baseline bill amount.

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- It is a reliable backstop that protects the least engaged customers from excessive standing offer rates. It is not meant to be the cheapest possible offer.

Together, these elements ensure the DMO remains both a robust consumer safeguard and a healthy reference point for market comparison. The DMO protects the most vulnerable without unduly blunting competitive signals.

Critically, the ACCC warned that the DMO should not be set so low as to become the de facto cheapest deal. Doing so would risk constraining genuine competitive differentiation, dampen innovation, and disincentivise active customer participation; it would disincentivise engagement.

The DMO is also not relatable to a significant portion of customers on market offers, including those with rooftop solar and the growing number on unregulated tariffs. The DMO does not accommodate emerging proposition models such as subscriptions, dynamic tariffs, or offers that reward flexible demand. And yet these are increasingly relevant as the system decentralises.

The DMO framework is currently fit for purpose in addressing the ACCCs original concerns about misleading discounting and opaque standing offers. In this regard, the DMO remains a consumer safeguard.

Going forward, the DMO's pricing basis should remain founded so as not to disincentivise retailers from offering innovative or tailored CER or other emergent energy solutions. Being compelled to conform to regulated structures or innovators being perceived as less competitive by poor comparators are serious risks that accompany setting benchmark tariffs.

Recommended approaches to keep the DMO Fit for Purpose:

- Keep the core "price ceiling and common discount baseline" design that has demonstrably reduced headline discounts.
- Ensure the DMO is not set so low that it becomes the cheapest offer, so as not to blunt genuine competitive differentiation.
- Consult on an "exemption pathway" for non-standard products (e.g., CER subscription, dynamic pricing offers), allowing innovators to operate outside rigid volumetric reference rules while preserving core consumer safeguards.

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3. Reference Price Function

Q3: How successfully does the DMO framework achieve its objective in being a reference price to allow customers to compare market offers? Are there any issues preventing the DMO in achieving this objective?

Response:

The DMO in its current format—an annual cost at model usage—has some limits of effectiveness for households with atypical consumption. Comparison for customers with controlled loads, demand tariffs, or comparison for CER products requires consideration. The purpose of comparison should be to facilitate interest in further innovation and differencing, and not to have all products available aggregate to a single comparison point. Retailers should lead in delivering tailored, understandable energy products.

The DMO and the associated "reference-bill" rules came into effect on 1 July 2019. The conditional-discount cap rules came into effect on 1 July 2020. Once these were in place, the average size of the headline discounts offered by retailers (measured against the DMO reference price) fell well below the average headline discounts they were offering against the old standing offer benchmarks:

- Pre-DMO legacy offers (mid 2019) commonly carried conditional discounts of 20 to 30 per cent. The ACCC found that "until recently, the majority of offers in the market included conditional pay-on-time discounts set above 20 per cent", with realised rates averaging around 27 per cent on legacy contracts.[15]
- New contracts post 1 July 2020 are subject to the AEMC's "reasonable-cost" cap on conditional discounts, meaning retailers can only set their pay-on-time discounts equal to the direct cost savings from late-payment risk. In practice, these discounts have tended to settle in the 10–15 per cent range against the published DMO reference price, reflecting the ACCC's objective to limit them to reasonable costs.[16]
- ACCC monitoring confirms this shift: in its December 2023 NEM report, the ACCC noted that customer-weighted average conditional discounts (measured against the DMO) were around 16.5 per cent, well below the 27 per cent of legacy standing-offer discounts pre DMO.[17]

[15] AEMC (2020) Final Determination Information Sheet at https://www.aemc.gov.au/rule-changes/regulating-conditional-discounting p.1

[16] The AEMC noted that the diversity of retailer costs, types of conditional discounts pricing structures and different business models would make it unlikely that the AER would be able to set a single level of reasonable costs.

[17] ACCC (2023) Inquiry into the National Electricity Market December 2023 Report at https://www.accc.gov.au/system/files/accc-inquiry-national-electricity-market-december-2023-report_0.pdf

Combined, this shows a clear structural drop in discount sizes once the DMO framework and the AEMC's conditional-discount cap rules took effect. Discounts measured off today's DMO are consistently lower than those that were measured off the old, pre-2020 standing-offer prices.

The retail component is relatively small across both the VDO and the DMO in any case, even with some minor differences in methodology. Any alignment of the methodology used to calculate retail costs and margin will have less impact than changes to other components of the cost stack. We note that between DMO4 to DMO7, retail costs and margin added $55 to a single rate NSW bill, wholesale costs added $250, and networks added $200.

Differences in wholesale prices and network costs also determine the quantum and longevity of market offers that sit below regulated benchmarks in every jurisdiction. The ability of smaller retailers to access competitive wholesale rates is a significant driver of whether there are market offers below regulated benchmarks.

Recommended approaches to the Reference Price function:

- Encourage the development of tailored, transparent comparison tools (e.g., online calculators that model actual usage patterns or customer CER profiles) to help and encourage customers to see the true value of dynamic and non-volumetric offers.

4. Efficient Pricing Framework

Q4: Should the DMO be set to reflect the efficient costs a retailer might incur in supplying electricity to its customers?

Q5: How does the inclusion of a competition allowance level the playing field between retailers, given the current market structure (specifically, considering the high-level of concentration of customers across the Tier 1 retailers, coupled with the significant customer disengagement prevalent in the market)?

Response:

The problem with an efficient pricing framework is its misalignment with the dynamic markets that retailers operate in. Static efficient cost models like that proposed for the DMO struggle to keep up with dynamic market shifts, such as decentralising energy, the emergence of new customer classes like "prosumers", and even electrification and decarbonisation policy shifts. These dynamic intersections create the potential for cascading failures and bankruptcies. A focus on service outcomes, not just cost inputs, might assist.

In levelling the playing field, not all retailers are equal, due to their structural, operational, and strategic differences. New entrants must spend more on marketing, advertising, and promotions to build awareness, and they will lack economies of scale. Their fixed costs (e.g., call centres, digital platforms) are spread across fewer customers, which means a higher cost-to-serve per customer, especially in the early stages. A cost-reflective DMO as described could disproportionately disadvantage retailers with legitimate but higher than average costs. This could lead to:

- Reduced product diversity
- Exit of smaller or higher-cost retailers (who are likely to be additional CER integrators and orchestrators)
- Market homogenisation, undermining innovation and consumer choice.

Smaller retailers also face barriers beyond pricing, including access to hedging products. Therefore, the allowance alone does not level the playing field. Retail competition not only has cost to serve and product differentiation benefits, it also supports generation investment. Retail competition supports wholesale contracting, hedging strategies, including small generation and batteries, all of which deliver benefits to all consumers.

All consumers benefit from effective retail competition, which is why we see merit in retaining it as one of the core DMO policy objectives. This benefit also accrues to those consumers who do not participate frequently and remain on, or close to, standing offer prices. Firstly, because they *can* access a market offer at any time. Details of better offers are now shown on all bills in NECF jurisdictions, and we have observed the effectiveness of this, especially in NSW. IPART's Monitoring the NSW Retail Energy Markets 2023-24 (Final Report released 18 December 2024) states:

> *"We found that in 2023-24, more consumers in NSW switched energy retailer or plan, and new and innovative energy products and services continued to emerge."*[18]

Secondly, competition creates a strong incentive for retailers to minimise all the costs in their cost stack. This includes their cost to serve and other operating costs, bad and doubtful debt costs, and environmental and wholesale costs. This does flow through to the DMO, since retailers report actual costs to the AER, and the AER uses this information to set regulated allowances.

[18] IPART (2025) website reference (summary box) at https://www.ipart.nsw.gov.au/review/energy/monitoring-nsw-retail-energy-markets-2023-24

Any focus on efficiency should also extend to network costs, given their contribution to the cost stack. This includes the efficiency of their operations, and whether there is a capex bias creating under utilisation rather than optimising existing assets. We also note the NSW Roadmap added almost $500m to the network component of the current DMO.

Finally, the direct policy or market reform outside the DMO framework and within the Nelson Review is also an important contribution here and the relevance of the DMO should be considered within that broader framework. And therein it is in the interests of consumers to preserve incentives for competition, not to eliminate them.

Recommended approaches to align pricing with efficient and dynamic market signals:

- Commence the necessary transition from static "efficient cost" models toward frameworks that can accommodate:
    - Locational network charges
    - Time-varying wholesale prices
    - Ancillary services and demand-response value streams.
- Embed the flexibility to update cost inputs mid-period if cost fundamentals shift materially, such as a major capex program or sudden changes in wholesale price drivers.

Recommended approaches to leverage the Competition Allowance:

- Maintain an allowance component in the DMO that:
    - Reflects smaller retailers' higher marketing and fixed costs.
    - Supports continued new entry, product diversity (like CER orchestration services).
- Complement this allowance with non-price measures to preserve competition, such as:
    - Pathways to easier access to hedging products for small retailers
    - Removing comparison barriers to new service offerings.

5. DMO vs VDO Comparison

Q7: How does the DMO framework compare to the VDO in terms of balancing consumer outcomes while maintaining competitive retail markets?

Q9: How has the exclusion of headroom for competition impacted the Victorian market? What are the key reasons why the headroom should be included in DMO regions considering it is not factored into regulated pricing in Victoria?

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Response:

The DMO framework delivers numerous market offers that are below the DMO, and many consumers, particularly those in hardship programs or receiving other forms of support from their retailer, are able to access them.

Regulatory measures that support access include the Hardship and Better Bills Guidelines, which are further complemented by recent AEMC determinations on rule change proposals to ensure consumers in hardship programs pay no more than the best offer. Now the DMO coexists with hardship and payment difficulty obligations, and support is available to any consumer who asks for it or is able to be identified as requiring it, although the DMO cannot address disengagement by itself. Payment difficulty frameworks are also targeted and effective ways of supporting vulnerable consumers. For example, retailers must attempt to identify and offer support to those experiencing payment difficulty, understand their needs and preferences, and then discuss cheaper and more appropriate offers with them.

The AEC still views the hardship frameworks as the most effective mechanisms for supporting those consumers and consumer classes who face unique obstacles to participating in the retail market. Policymakers, regulators, and the consumer sector can support this by building trust in the retail sector and awareness of regulatory entitlements, such as the availability of support. The AER's forthcoming review of the Hardship Guideline is a further opportunity to identify reform opportunities. We acknowledge that more can be done to assist and expand on this after the Questions.

Effective retail competition also creates a strong incentive to innovate in order to win and retain customers. This, in turn, will support the energy transition; retailers developing service offerings that help owners of CER to maximise the value of their investments and other consumers to manage risk in more innovative ways (e.g., shifting their consumption to avoid sharper price signals). Creating the market enabling products that lead to a more efficient and lower cost system, improving outcomes for all consumers.

The problem with comparing this to the VDO is that the alignment of the methodology for calculating retail costs with the VDO is not, in itself, delivering significantly lower prices nor completely suppressing innovation and retail competition, given its relative contribution to the cost stack. The state of generation and wholesale outcomes in each jurisdiction is a more important factor here.

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The VDO, which excludes headroom and is based on efficient costs, has been suggested to have maintained competition, but there are other variables to the total retail sale price that have impacted Victoria:

- Victoria's wholesale electricity prices have been notably lower than the national average, and renewable energy sources have contributed to this.
- Network costs in Victoria are lower and comprise a smaller proportion of residential bills than in New South Wales and Queensland.
- Victoria will see a more modest increase in distribution costs this year compared with other NEM states.

A regulator could face uninformed risk in attempting to replicate Victoria's competitive outcomes by pulling the lever on the competition allowance and efficient pricing methods only. The VDO does not prove that competition can thrive without headroom alone, without taking account of other factors.

Recommended approaches to learn from Jurisdictional differences (DMO vs VDO)

- Consider the comparative study of retail cost stacks between Victoria (VDO) and DMO jurisdictions provided in submissions to understand:
    - Network vs wholesale-driven price differences
    - Where any practical effect of headroom exclusion on competitive outcomes can be attributed.
- Use those insights to help calibrate the DMO and VDO differences, rather than assume that Victoria's headroom-free model alone explains lower prices.

6. Innovation

Q 10: What specific innovation has been delivered through the introduction of competition in the retail electricity market? What specific innovation has the inclusion of the competition allowance fostered in the market?

Q 11: Is price dispersion of market offers a meaningful area of focus in the context of considerable customer disengagement in the market? What drives price dispersion in retail electricity markets, and how much price dispersion is driven by competition, in comparison to other drivers?

Response:

Retail competition is viewed unfavorably by some, but it has driven huge steps forward. Only two decades ago, most people got one paper bill every three months with little visibility into how or why their costs had changed, whereas today the competitive retail market offers:

- Choice and tailoring of pricing
- Green-energy products (100% renewable, carbon-offset bundles) for those who want to minimise their footprint
- Flexible pay options
- Real-Time Information & Control, with dashboards and mobile apps showing daily or even up-to-the-minute information
- Alerts and bill-forecasting tools so you are never surprised by a spike
- Easy online switching tools to compare and move between offers in minutes
- Value-Added Services like solar-and-battery bundles, electric vehicle charging plans, and demand-response programs that reward you for shifting load
- Home-energy audits and smart-home integrations
- Loyalty rewards, referral bonuses, and bill smoothing plans to help manage cash flow
- Better engagement and support with targeted assistance for vulnerable customers with hardship programs and tailored support packages
- Educational content, energy-saving tips, and usage comparisons to peers.

We need to take a broader account of this in a reasoned way; it is not just the discrete amount of the competition allowance that should be considered. All of this is competition-driven innovation, even where it has been a policy direction - competition-driven implementation gives the best customer experience. A better experience than rivals. Competition means that engaged customers now can not only see what is happening near-real time, but choose exactly the mix of pricing, services and green credentials that match their needs. Compared to the quarterly paper bill era, customers are no longer simply passive payers in the energy market; they can also be empowered participants.

Now, there is limited evidence that the competition allowance itself, as opposed to competition, has driven innovation beyond standard pricing strategies. This is because innovation in that case can be better linked to technological developments than to the DMO structure. Most innovation, such as app-based management tools, has logically occurred across all jurisdictions, including in Victoria, where no allowance exists. But it has had to be paid for; there is no such thing as a cost that does not find its way through to the consumer. Victoria may simply have been an economic “free rider” to innovation, but not all participants can be free riders and still get innovation.

Expected returns to retail operations are also a factor in driving innovation. Retailers need to have confidence that they can take risks to develop innovative retail products (which may not always be

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successful) and then share the additional value they create with their customers, while earning a return on investment. The current and future level of the DMO is clearly a factor in decisions on expected returns. In the AEC's view, the DMO is one element of a broader framework that influences innovation. But the innovation allowance is still an important one.

Pricing strategies are important. Whilst policy examples that can influence innovation include the accelerated rollout of smart meters (ASMR) program and the Commonwealth Government's CER roadmap, it is pricing innovation that will be the product of ASMR, or the crucible for the CER roadmap. Pricing innovation is important. The AEMC's current review of pricing is considering whether further reforms are necessary for network tariffs to drive retail innovation. We share the AEMC view that:

> "*Meeting preferences for the range of future consumers, including those with and without CER, will require diverse offerings of products, services, and pricing structures.*"[19]

The AEMC emphasises a need for consumer-centric pricing and electricity pricing structures that reflect the evolving preferences and needs of consumers. This includes offering a range of pricing options that accommodate different usage patterns and technological capabilities.

Under the current DMO framework, where the DMO functions well as a reference price, the DMO is a useful tool for consumers comparing products with simpler tariff structures. Because comparison with the DMO involves arbitrary assumptions about the use of CER and the timing and volume of consumption, it is unlikely to be useful for consumers who either have CER or who are willing to respond to sharper signals. That's ok; the DMO can still influence innovation without driving every aspect of it. There is a broader framework, and the DMO cannot be expected to do everything, but its impact on the broader framework is still important.

Research on price dispersion in other markets suggests that competition typically contributes no more than 10–15 percent of the observed price dispersion. The balance of price dispersion is driven by variations in input costs, and just by divergence across sellers and consumer types.

In retail electricity, where 40% of the input costs are regulated, price dispersion is potentially an even more valid competition metric, and perhaps competition could be up to 30% of the reason behind observed price dispersion in electricity on that extrapolation. Price dispersion is one of many measures

[19] AEMC (2025) The Pricing Review Discussion Paper at https://www.aemc.gov.au/market-reviews-advice/pricing-review-electricity-pricing-consumer-driven-future p.28

that inform assessments of competitive markets internationally, and it is probably not conclusive in isolation. Nevertheless, it is entirely relevant in a market where 80% of customers have engaged. So, whilst the DMO's role should be to provide a simple and fair baseline, the DMO should not have the consequence of stifling a wide range of pricing options above that baseline.

Price dispersion can deliver good outcomes if those who are most sensitive to price can benefit from and access the cheapest market offers. The current policy framework is delivering market offers below the DMO, but we acknowledge the legitimate concerns that some consumers are not well placed to access them. The practical effect of price dispersion is that it can deliver good outcomes if those who are most sensitive to price can benefit from and access the cheapest market offers.

Retailers understand that markets with price dispersion in which customers pay different prices for similar services can risk losing public support if vulnerable customers consistently pay more. Ensuring vulnerable customers access the lowest prices helps and is an objective for retailers.

Recommended approaches to drive innovation

- Retain an explicit "innovation allowance" (or equivalent) within the DMO to ensure retailers can fund expansion of service offerings, consumer apps, and platform enhancements.
- Lower comparison barriers to encourage competition in service offerings, such as:
    - Demand-response programs, CER subscription bundles.
    - EV charging plans, loyalty rewards.
- Monitor non-price innovation metrics as well (e.g., the scope and number of CER integration products) alongside traditional price-dispersion measures.

Recommended approaches to Price Dispersion:

- Track price dispersion to gauge how much is driven by competition versus input cost variance; avoid policy levers that artificially compress or widen spreads.
- Continue to ensure that the cheapest offers remain accessible to those most sensitive to price (e.g., via outreach, hardship programs, proactive offer notifications).

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