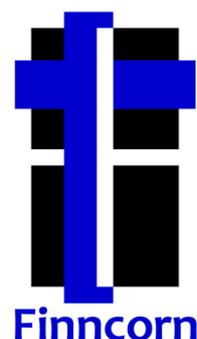


13th February 2026

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AEMC Pricing Review – assessing impacts of Recommendations 1 and 2

You asked Finncorn to examine the AEMC's draft report from their Pricing Review, with a particular focus on their Theme 1 – *“Harness competition to improve outcomes for all consumers”*.

Under this theme, the AEMC are making two very significant Recommendations which would materially alter retail competition, pricing and consumer experience. We summarise these as:

R1 – ‘Same plan, same price, no loyalty tax’

R2 – ‘Auction off disengaged customer cohorts’

We have prepared the following paper based on our understanding of the nature of retail competition in electricity markets. In our view, much of the rationale for these recommendations goes back to issues we analysed closely for ECA in 2017, to help inform the ACCC's Retail Electricity Pricing Inquiry¹ and which were adopted by the Victorian Essential Services Commission in its consideration of the benefits (or otherwise) of the competitive retail market at that time.²

We provide our brief thoughts on how ECA might consider the consumer impacts of these recommendations, including some suggestions on how the detailed design of these reforms might assist in achieving the objectives the AEMC has stated in theme 1 above.

We understand ECA may choose to incorporate this paper as part of its public submission.

Yours sincerely,

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¹ Still available here: <https://energyconsumersaustralia.com.au/our-work/research/state-play-quantifying-competitive-outcomes-retailing-nem>

² For example: <https://www.esc.vic.gov.au/sites/default/files/documents/The-unfortunate-paradox-of-retail-energy-prices-20180625.pdf>



AEMC Pricing Review

Finncorn Consulting’s assessment of Recommendations 1 and 2 as presented
in the Draft Report

Released as a public submission

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Recommendations should be considered together...

Our reading of the AEMC’s materials including the Draft Report suggest to us that the intention here is to reshape (for the better) the nature of retail competition for small customers.

In doing this, we think the two recommendations in isolation would be far less effective than a well-considered version of both being applied.

This is because in many respects, effective retail competition is fragile, and the prima facie impact of R1 would be likely to threaten at least the external metrics that might indicate it exists. By contrast, a well-structured R2 could encourage and strengthen it.

What does good look like?

We regard competition as effective when it reveals the efficient cost to provide energy services to customers, without allowing for systematic excess returns to be earned within the retail industry.

In addition to this, competitive activity itself involves real costs, which are recovered from consumers – so more is not necessarily better.

There is an optimum where competitive pressures deliver the efficient outcome, but not to the point of driving up industry costs for little or no marginal consumer benefit in pricing or any other dimension of the service provided.

... and with an eye on replacing the DMO/VDO

We think the AEMC have an ambitious view that under these recommendations, there will be a reliable and regular indication of the efficient cost to serve cohorts of ‘basic’ residential customers – via the revealed pricing from auctions held under R2.

If that is the case, this price could form a market-based benchmark that could replace the administratively determined DMO/VDO equivalent. We tend to agree this would be a better outcome, with less distortion and regulatory risk for both retailers and consumers.

R1 – same plan, same price, no loyalty tax

These are some of the questions which we think consumer advocates should ask (and they or the AEMC should answer!) in relation to R1:

- How important is rewarding / encouraging consumer engagement, versus uneven pricing outcomes that tend to result?
- Are more even pricing outcomes regardless of engagement level desirable – is this a dimension of ‘equity’ that should be pursued through retail regulation?
- If so, is an improvement in equity alone a good enough reason to do this?
- How concerned should consumer stakeholders be about ‘output’-style measures of retail competition such as churn, quantity of retailers, and market concentration versus ‘outcomes’ – such as the average prices consumers face?
- Is R1 likely to reduce or raise industry costs?
- Regardless of the answer to the above, is R1 likely to reduce or raise industry profitability?
- There is a difference because the impacts on competition are relevant here – what would happen?

First order: Smoothing out retailer profits, not slashing them

Prima facie, given there is a differential between back-back / front-book profitability (aka a loyalty tax), narrowing or eliminating that via regulation would be expected to compress the range of gross margin per customer within a given retailer towards a narrower band.

AEMC Pricing Review – assessing Recommendations 1 and 2

That implies some winners (the disengaged), some losers (the engaged) but as a first-order effect, no net change in retail costs and margins.

This is the starting-point for thinking about R1, and there MIGHT be an argument that even this outcome is better than the status quo IF one or more of the following are true:

- An acceptable definition of ‘equity’ is that same product should mean same price³;
- There is no underlying suspicion that retailers are overearning via the status quo;
- It is considered worthwhile merely in order to reduce distrust in retailer offers and thereby increase customer satisfaction / engagement;
- It saves customers the time, effort and existential angst associated with comparing energy plans in search of large savings.

In other words, there is a fairly pessimistic scenario where all R1 does is shift rent from the disengaged to the engaged, but even that could be taken as an improvement.

Second order: Impacting structural costs

Beyond this, it is important to consider the second-order effect as well – what would such a regulatory structure imposed on retail pricing mean for retailer costs?

A reasonable hypothesis is that a large proportion of observed churn is driven by price-based competition, that is in turn funded by the loyalty tax. In this case, R1 would mean lower churn.

Competing is expensive (see our prior work on this via footnote 1).

As a result, industry-wide retailer costs could be materially reduced if there is a general reduction in competitive activity – via lower customer acquisition and retention costs.

In addition to this we might also see chunks of fixed costs come out of the industry, as retailers totally dependent on the loyalty tax as their strategy fail.

Countering this, the regulation itself would introduce material transitional and ongoing compliance costs, both within retailers and the AER, which would be recovered from consumers.

We don’t think the transitional costs should be over-emphasised, but it would be important to have a view on the net effect on structural ongoing costs. This would require proponents of R1 to opine on:

1. How much will churn decline?
2. How much operating cost will that remove from retailers?
3. How many retailers will exit?
4. How much fixed cost will that remove from the industry?
5. What are the offsetting new costs?
6. What is the net impact on structural retail electricity industry costs?

Simple!

Third order: Impact on competition and thus profitability / consumer costs

By this stage we would have a view on the efficiency of R1 – and for the sake of the argument let us assume it would be expected to structurally lower the overall industry costs by some meaningful amount.

The extent to which consumers see any benefit passed through as lower prices relies on the effectiveness of retail competition, and this is another question entirely.

What we can observe is that the status quo has provided a mechanism for new-entrant retailers to establish themselves, and for all retailers⁴ to compete and (in some cases) grow their customer base.

³ One might equally argue that ‘equity’ mean those who shop around, benefit. Others would note the practical impediments of complexity in doing so, for what is an essential service.

⁴ See our Appendix for a summary of retailers and their residential customer number trends over the past five years.

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Therefore, it seems reasonable to assume under R1 there will be less of this competitive activity (without opining on whether that is good or bad for consumers).

We think it is highly-relevant to observe that smaller retailers are fundamentally higher-cost than large ones⁵, largely due to:

- Scale effects of fixed costs
- Benefits of vertical integration for larger retailers
- Higher hedging costs for smaller, less-creditworthy retailers

This can be papered over by small retailers, if they are prepared to really work the ‘loyalty tax’ – barely-profitable front-book offers to gain customers, with an expectation that the back-book quickly starts to fund this. R1 kills this strategy. The AEMC’s recommendation would likely force smaller retailers to price accurately to their costs (including the need to offer a return to their capital providers – aka a profit).

As a result, some common measures of competition are likely to deteriorate – including churn rates, the number of retailers active in the various markets, and the concentration of the retail energy market.

We may see an apparent shrinkage of the industry down to a smaller number of retailers from the current 56, with each serving (on average) a larger customer base. Depending on the extent of this effect, that may reduce competitive pressure on larger retailers.

Therefore we think it is reasonable to suspect the third-order impact of R1 could be – in a more pessimistic case:

- Less dispersion in customer prices, but similar overall customer revenues
- Higher overall retailer profitability via structurally lower competitive costs AND structurally lower competition to place pressure on margins.

There is a more optimistic view, which becomes related to R2. Competition ‘post-R1’ could prove to be equally (or hopefully, even more) effective than it was before.

This relies on a view that in fact, the simplistic measures of competition are not really relevant, especially if a cohort of small, inefficient ‘Tier 3’ retailers tend to set the marginal price at a level that is related to their higher cost base, not that of the larger, more efficient retailers.

On this view, the loss of some small, inefficient retailers who were overly reliant on the pre-R1 loyalty tax strategy is no concern for consumers.

Competition would be no less effective, and lower industry costs resulting from R1 would be passed through.

Fourth order: The replacement of competition... maybe?

What next for retailers and retail competition, after the old loyalty tax playbook is lost?

Retailers will still have the urge to gain customers – might this lead to better competition on other dimensions (as the AEMC clearly hopes)? We can dream up many possibilities – competition driven by:

- Service quality
- Product / tariff design
- Better customer segmentation (as AEMC notes, ‘family plan’, ‘retiree plan’, ...)
- Co-benefits & perks
- Loyalty schemes

Many things are possible, but it might also be worth considering how much there really is to play for here, before placing too much credit on this potential outcome. Sceptics might ask themselves:

- What are the real gaps and opportunities for customers to be ‘delighted’ by a relationship with an energy retailer to ensure the light comes on when the switch is flicked?

⁵ We analyse and discuss this, and its implications for retail competition, at length in the reference in footnote 1.

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- What are the mythical new and better product designs that have eluded the market to date only because retailers have instead been focussed on price?
- Are these really likely to drive the necessary levels of customer engagement and thus maintain adequate competitive pressure on retailers?
- Would this just reintroduce new competitive costs to be recovered from customers, negating any benefit from structurally lowering industry costs?

Another potential outcome is just a quieter, more boring landscape of retail energy offers, with less consumer engagement and less of the traditional version of competition (for better or for worse).

R2 – auction off disengaged customer cohorts

We understand the premise here is that customers who have – via disengagement or other misfortunes – ended up on a Standing Offer tariff ('SO') would gain from being competitively auctioned off, to receive a price level below status-quo SO prices.

And again, the starting-point should be that:

- whatever the 'loser' retailers give up in higher-margin SO customers (a part of the back-book being attacked in R1) they will seek to make up via their pricing to other customers; and
- whatever the 'winner' retailers bid to take on the OS cohort, it will be accommodated within overall pricing and profitability for that retailer's total customer base.

As a result, many first-order impacts are the same: less price dispersion, arguably greater equity, customer trust and satisfaction. But also, less reward for those customers who do or have engaged.

As we did for R1, we have to then ask: Is that it, or are there other benefits or disadvantages?

Interesting opportunity for a growing retailer to get scale

There is a large cohort of SO customers – roughly 9% of all residential customers, or about 920,000 accounts, based on figures from the most recent DMO and VDO processes.⁶ They are almost twice as prevalent in Victoria compared with other competitive NEM regions.

We assume (as this is a level of detail not yet revealed by the AEMC) that:

1. Auctions would be held for cohorts of customers at either regional or DNSP level, in which case the biddable item would be a customer base of tens or hundreds of thousands.
2. Auctions would not be a one-and-done event, but repeated (annually?) as new customers fall into this unfortunate situation.

If so, **this process could be very pro-competitive** in our view.

The cohorts would represent a material customer acquisition opportunity that could help a smaller or mid-sized retailer gain material scale and reduce their unit costs, making them a more effective competitor with the 'Big 3', who each have several million customer accounts. This could include encouraging new-entrant competition into some areas of the NEM where competition is severely lacking, including Tasmania, the ACT and north Queensland.

The cost to acquire (via participating in the auction process) would likely be a lot less than the traditional grind of acquiring one-by-one via advertising costs and direct marketing engagement. For example, if an organic acquisition cost is in the order of \$200, then it seems clear the administrative cost to participate and acquire 100,000 customers under such an auction would be orders of magnitude less than \$20m.

⁶ ECA notes there are 475,727 (8.2%) residential and 91,060 (17.6%) small business in DMO regions: [Default market offer prices 2025–26: Final determination](#) p 15, and 445,000 households (15 per cent) and 54,000 small businesses (19 per cent) for the VDO: [PPR - Request for Comment Paper - 2026-27 Victorian Default Offer - 20251114_0.pdf](#) p 4

Standing Offer customers are relatively docile by definition...

The SO cohort have demonstrated their disengagement with the competitive market already, making them a relatively attractive cohort to acquire – because they are unlikely to churn away of their own volition.

All else equal, this makes them a more valuable customer to acquire.

... but that becomes a two-edged sword!

Unfortunately, the risk is that what is won can be lost, if the customers fall onto another disengaged plan and are simply re-auctioned. This has a couple of implications:

1. If the ‘customer life’ might be as little as one year, a winning retailer might need to price in cost-recovery for the auction process over a short period, perhaps increasing the tariff level they are prepared to offer.
2. If winning the cohort offers scale and reduces fixed costs per customer, the reverse is also true: losing them a year later could initiate a further loss of competitiveness. This would be particularly acute in cases where the acquiring retailer’s customer base is relatively modest compared with the size of the acquired cohort.

Perhaps this suggests both retailers and the AEMC / AER (in designing the process) should be open to a longer life for acquired SO customers with their new retailer, even if they insist on remaining disengaged.

It might also give reason to consider whether the long tail of very small retailers, most susceptible to the second effect above, are likely to take on the risk of sudden but potentially short-lived growth. As we note below, pre-qualification of retailers deemed to have the necessary capacity may be warranted.

What are the risks to a pro-competitive outcome – and how to mitigate?

Our thesis is that the larger retailers have advantages in their cost to serve – and if that is the case, might the result be the Big 3 gentailers simply outbid Tier 2 / Tier 3, further advantaging themselves at the expense of effective competition?

In short: yes, this is a clear risk. Is this actually a bad thing for consumers overall? That is a bit more subtle.

It would be bad if:

- (a) competition among the Big 3 was not adequate to reveal the most efficient cost in bidding; and
- (b) the effect meaningfully impeded competition outside the Big 3.

It might not be so bad if (a) was false, even if (b) was true. In that event, SO customers would receive the best price available.

This risk could be mitigated via auction design – for example, conditions of an auction might include:

- **Exclusion of dominant bidders** – perhaps the top [2] retailers by market share, or any retailer with a market share already exceeding [20%] in the relevant region or DNSP area.
- **Pre-qualification based on retailer’s capacity** to integrate and serve a large cohort (to eliminate the least-capable bidders, including very small / inexperienced retailers).
- **Pre-arrangement of a hedge position**, to be novated across to the winner.
- **Splitting the cohorts** – with a guarantee of more than one winner per auction.
- **No auction without [4] prequalified bidders.**

There are numerous pros and cons that would need to be weighed up, which in many cases would be balancing overtly pro-competitive market design (to encourage healthy long-term competition) at the expense of the cheapest possible price on the day for the SO customer (the short-term competitive outcome).

Stalking horse to kill off the DMO / VDO

While the discussion above should make clear it is far from guaranteed, we do think there is a world where SO auctions might reliably and regularly reveal the efficient cost to serve a ‘basic’ retail electricity customer.

This seems to us to be the real objective of the DMO / VDO. If that is the case, we think it is very reasonable of the AEMC to wonder whether both are needed.

There are many challenges with the DMO / VDO, especially the process of setting it annually based on assumptions about costs and the future:

- Should it allow for competitive costs, or not – in other words, should it encourage competition, or not?
- Should it be based on the lowest cost to serve, or the median, or a high-cost new-entrant, or...?
- Exactly how wrong will its assumptions on the future wholesale / hedging costs be, and how much damage will that entail for retailers or consumers versus a competitive market outcome?

In fact, perhaps the best way to assess R2 is as:

1. a planned replacement of the DMO / VDO with a competitively-determined alternative – an idea which appears to have a lot of merit to us; AND
2. an offset to some of the damaging impacts R1 is likely to have on retail competition, at least as we know it today.

Customers (and retailers) would have a number of concerns

From a customer perspective there are clearly some concerns to be thought through.

- Is it really OK to change a customer’s retailer out from under them?
- What if some customers consciously remain on a retailer’s SO for other reasons – not price-sensitive, but valuing other things (brand, carbon intensity of supply, ...?)
- Should customers have to opt-in to be auctioned?
- Or if not, can they opt-out?
- What if they are dual fuel or NBN customers of the retailer in question?
- What happens to those customer’s debts to their current retailer – do they transfer too? Or does the outgoing retailer send in the debt collector?

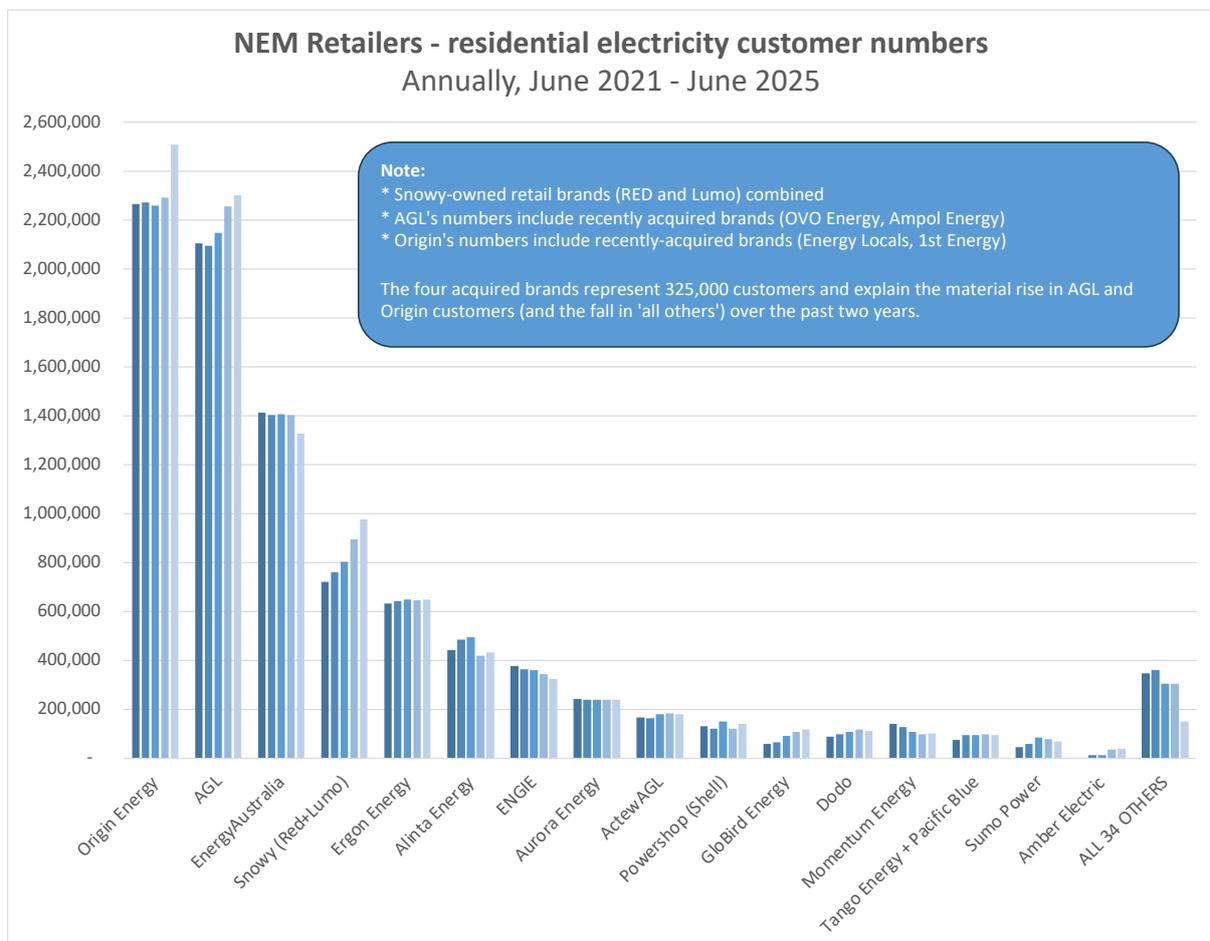
There are a lot of trade-offs here for consumer stakeholders to consider. Some could be designed around to become acceptable, but others are pretty fundamental: including a premise that someone else knows what is best for these consumers, and feels strongly enough about it that they are prepared to change their commercial arrangements on their behalf.

Appendix - Retailing structure in the NEM

Retail customer numbers are reported quarterly to the AER and the Victorian ESC, but some care is needed in assessing the bare data. This is due to a number of cases where multiple brands under a single owner are reported separately, as well as several quite recent acquisitions of smaller retailers by the Tier 1 players AGL and Origin.

In assessing how an auction of SO cohorts might fit within the competitive dynamics of the NEM, we think it is important to adjust for these factors – the chart below does so by:

1. Combining the two Snowy-owned retailers, Red and Lumo, into a single (quite large, and rapidly-growing) figure.
2. Adding into AGL's numbers their 100%-owned (and growing) OVO Energy brand (112,000 customers), as well as the recently-acquired Ampol Energy cohort (51,000 customers).
3. Adding into Origin's numbers the customers recently acquired from 1st Energy (64,000) and Energy Locals (96,000).
4. Combining Tango Energy and Pacific Blue, two Tier 3 brands both 100%-owned by China's SPIC.



Source: AER and Victorian ESC data, Finnorn analysis

Once adjusted, we find there are 50 distinct retailers serving 9.8m residential customers in the NEM.

- The **three Tier 1 gentailers** – AGL, Origin and EnergyAustralia – account for 63% of the customers (unchanged over the past 5 years), with an average of 2.05m customers each (in fact, EA is substantially smaller at 1.3m)

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- There are **seven Tier 2 NEM retailers** if the cutoff is > 100,000 accounts, or about 1% market share. Collectively these hold 22% of the market at an average of 315,000 customers.
 - The largest of these, the Snowy retail brands (RED + Lumo) have about one million accounts and have been growing rapidly towards joining Tier 1.
- There are **three regional specialists** – Aurora in TAS (92% share), Ergon in QLD (29% share overall, dominant outside SE Qld) and ActewAGL in the ACT (72% share). They have between 180,000 and 650,000 accounts so are ‘Tier 2’ in size.
- The remaining **37 Tier 3 retailers** collectively hold only 356,000 accounts, or 3.2% market share – an average of under 10,000 customers each.

In this context, the ~920,000 SO customers are a large cohort, much larger than the customer base of most retailers. If (for example) auction processes split these into (perhaps DNSP-defined?) chunks of ~70,000 customers, then there are only 14 retailers NEM-wide for whom that would be less than a doubling in size. If (for competitive reasons) the Tier 1 retailers and regionally-dominant retailers were excluded, this number would fall further.

However, we think this data shows there is still a reasonable cohort of Tier 2 retailers who may offer effective competition while having the capacity to absorb customer portfolios of this size.