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2026–27 Victorian Default Offer: Request for Comment Paper

Essential Services Commission Victoria

Submission via email: **vdo@esc.vic.gov.au**

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AGL Response to 2026–27 Victorian Default Offer: Request for Comment Paper

AGL Energy (**AGL**) welcomes the opportunity to comment on the 2026–27 Victorian Default Offer: Request for Comment Paper (**RFC Paper**).

The energy market is undergoing a generational transformation to a more modern and productive system, with lower emissions. The digitalisation, decentralisation, decarbonisation, and democratisation of the energy system is changing market dynamics and requires retailers to underwrite significant investment in new infrastructure and systems for the benefit of customers and the broader economy.

An efficient VDO is essential to enable a timely, fair and orderly transition, and a key focus of any adjustment to the VDO methodology must be to ensure that a prudent and efficient retailer remains viable – that is, able to meet all costs and enable returns on investment that enable it to support the finance required to fund the provision of better energy services to customers. Retailer viability is essential to deliver good customer outcomes and to ensure the financial stability of the energy supply system.

As AGL has submitted in response to previous consultations on the VDO methodology, the retail margin provided for in the VDO methodology is presently too low to be sustainable and efficient to provide the best long-term outcomes for customers.

Retailers ultimately fund all costs and investment through the energy supply chain, including network costs and generation. Retailers are also exposed to significant price and volume risks. The VDO sets a regulated fixed price that a retailer must sell electricity at in the future, even though retail costs are variable and, in the case of wholesale electricity costs, extremely volatile. A prudent retailer must ensure it has hedging and funding arrangements in place to manage all credible price outcomes.

Stability, predictability and viability are critical to delivering a fair, trusted and reasonable price for the supply of an essential service. The VDO must be set at an efficient price in the long-term interests of consumers.

An efficient VDO price is even more important following a recent decision from the ESC, which means that the VDO price will effectively apply to more customers (including more market customers) [1]. Accordingly, the VDO will effectively set prices for a significantly greater proportion of customers in Victoria. The broader reach of the VDO must be considered when determining the VDO and how it will impact the overall market and long-term interests of consumers.

[1] Retailers will be required to ensure that customers on older contracts are paying a 'reasonable price' for energy. While the 'reasonable price' requirements do not directly require the application of VDO price outcomes, the VDO will likely become an important consideration when determining what is a 'reasonable price', noting that a price below the VDO is deemed to be a reasonable price under the Energy Retail Code of Practice.

We acknowledge the Victorian Government and ESC's motivation to consider the possibility of a free power period tariff in Victoria, and we welcome the Victorian approach to consult prior to deciding on whether to implement a regulated free power period offer.

AGL is uniquely placed to comment on free power periods given our market leading innovation delivering free power period products offered by AGL and its subsidiary OVO Energy. AGL is proud to have led this innovation to meet emerging market and customers' needs, including sharing the benefits of solar with customers who face barriers to installing their own. The benefits of innovation and competition to customers are significant and can be seen in this increasing diversity of offers provided by retailers in the market.

However, these innovative market plans are early in their lifecycle, and we believe it would not be appropriate to build 'free period' plans into the regulated pricing structure. The cost reflective time of use VDO is fairer and more sustainable and efficient for a regulated pricing structure.

A regulated free power period risks significant unintended consequences for customers, including impacts to power quality requiring expensive network augmentation and introduction of new unfair cross subsidies. The risk of adverse consequences is particularly high in Victoria due to the relatively low solar output in winter combined with concurrent electrification of winter heating loads. While we expect these risks can be effectively managed through flexible design and communication of market offers as they scale, this should not be expected for regulated free period offers that are inherently less flexible and result in less diversity in load-shifting. We encourage the ESC and Victorian Government to engage further with Victorian DNSPs on potential risks and challenges to distribution networks.

More information in response to this proposal is included in the **Attachment** to this submission, as well as our response to other questions raised in the RFC paper.

In summary, AGL:

- Supports the ESC largely retaining the current VDO methodology, however the retail margin is unsustainably low.
- Supports inclusion of the allowance for the wholesale electricity cost of exports.
- Supports the VDO continuing to align with distribution tariffs and transitioning to include the new solar soak period as an efficient cost reflective time of use tariff option for customers.
- Does not support the introduction of a regulated free power period offer in Victoria.
    - A regulated free period creates risks of unfair cross subsidies, power quality issues and unintended costs for network augmentation.
    - Significant challenges to the development of a regulated free power period offer include the need for clear opt-in processes, fair use controls, alignment with network tariffs and consideration of seasonal deficits, which may not be functional under a regulated VDO regime and standing offer framework.

If you have any queries about this submission, please contact [redacted]

Yours sincerely,

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AGL response to the 2026-27 VDO: Request for comment paper

AGL supports the ESC largely retaining the current VDO methodology. Although we have previously disagreed with several aspects of the current approach, we are mindful these are features of the VDO methodology that are not currently open for further consultation. In the interests of regulatory stability, certainty, and transparency, we therefore consider the VDO methodology should remain unchanged for the 2026-27 VDO decision.

Outlined below is our response to issues raised in the RFC paper.

Allowance for the wholesale electricity cost of exports

We support the ESC's current VDO methodology that includes an allowance for wholesale electricity costs of exports. With the regulated floor on retail feed-in tariffs, the negative value of some exported electricity will need to be absorbed by the retailer and therefore spread across all customers. This requires an assessment of the representative retailer's customer solar export volumes to derive a total cost of exports. Like other WEC components this will need to be translated into a $/MWh amount. The current methodology reflects this cost assessment approach.

We note this cost assessment may also need to include network import charges if the AER approves the DNSPs' proposals to include opt-in two-way network tariffs for residential customers.

Network Costs – residential time of use tariff with new lower cost solar soak period

Consistent with the VDO's established pass through approach to network costs, we support the continued application of the default TOU tariffs that will be in place during the relevant VDO pricing period.

We acknowledge that the VDO TOU network tariff structure will therefore need to change from a two-price period to a three-price period tariff. We do not consider there are material factors that require the ESC to alter this approach.

The suitability of a free power period tariff

AGL is uniquely placed to comment on the suitability of a regulated residential tariff with a free power period in Victoria given our market leading innovation delivering free power period products under AGL and its subsidiary OVO Energy.

Market plans that offer free power usage are still in early development and trial phases. Flexibility in the initial stages of development and product design are critical features of market development and enable rapid evolution to scale in response to uptake to manage unexpected challenges or cross subsidies.

Given these innovative plans in the market are nascent, and information that is still being analysed regarding challenges with their broader adoption, a regulated pricing structure with a free usage period would not be suitable for Victoria in the near term. There is insufficient data and experience to properly inform a regulated pricing structure that may scale to the broader market.

By design, a fixed three-hour free window moves a large share of discretionary electricity usage into the same time interval. There is a high risk of unintended consequences from the scale and inflexibility of a regulated free period, including impacts on electricity network power quality and costs from concentrated demand, particularly in the Victorian winter when combined with rapid electrification of heating and increasing uptake of home batteries and EV charging.

The cost reflective time of use VDO (which is proposed to include the new 'solar soak' period for the next VDO) aligned with distribution tariffs is a more appropriate and efficient regulated price that meets many of the same objectives as a free power period tariff without the additional risks.

In consideration of the suitability of a free power period product in Victoria, we have organised our feedback on implementation challenges and risks into three broad areas of discussion:

1. **Viable:** any regulated free power period tariff would need to have a sustainable pricing structure that reflects the cost of supply without reliance on unfair cross subsidies from other customers. This is consistent with the VDO principles and good regulatory practice.
2. **Doable:** a regulated free power period tariff is unlikely to be simple and flexible, and would likely create significant implementation cost, risk, and customer confusion if structured as a regulated standing offer.
3. **Safeguards:** fair use controls and consideration of network impacts would need to be prerequisites to protect customer experience, minimise unfair cross subsidies, and support a more equitable transition. A free power period tariff must be a voluntary 'opt-in' product for customers, and is better suited to a market offer.

A free power period product would need to be viable

The overall pricing structure for a free power period product would need to be sustainable and cost reflective, consistent with the VDO principles and good regulatory practice, to deliver the best long-term outcomes for customers. Retailers would need to be able to fully recover costs through the overall pricing structure of the VDO without reliance on unfair cross subsidies from other customers on the VDO or market plans. For this to occur, underlying cost drivers would need to be comprehensively understood and reflected in the pricing methodology.

Any free power period product must be an opt-in product for customers. Customers would need to make an informed and active decision to sign on to this product, especially as realising the customer value of these products primarily rests on the customer's willingness and ability to shift consumption to the free usage period.

A key challenge would be that there are material direct variable costs of supply within any potential free usage window. This introduces significant tariff design complexities as this cost is contingent on the amount of energy supplied during the free usage window and at other times.

While the average annual wholesale spot market value of energy in the middle of the day is regularly near zero in Victoria, customer consumption still incurs network, AEMO, and government scheme usage charges, costs, and liabilities.

Wholesale energy costs are also highly variable, and wholesale prices can be high even in the middle of the day because of several factors such as transmission or generation outages and constraints, or as a result of seasonal weather extending not only to temperatures but also wind and cloud cover.

In Victoria, as customers increasingly seek to electrify their heating load, there may be a shift towards higher prices in periods that have traditionally seen lower wholesale price outcomes. For example, among several other studies, AEMO has suggested that in Victoria, "with widespread electrification, peak demand may shift from summer to winter as heating demand surpasses cooling demand."[2] This is likely to result in changes to patterns in wholesale price outcomes on both as peak load shifts to meet winter demand.

While outcomes for Victoria wholesale electricity prices remain uncertain, both the broader VDO methodology and any proposed free power period product would have to include sufficient flexibility to ensure that consumption is encouraged at times that support the best customer outcomes but also the broader operation of energy markets.

[2] See, for example; AEMO, *Gas-Electricity Meter Data Linking Project Report*, January 2025 (available here)

Costs incurred by customers on a free power period tariff would have to be able to be recovered from those customers, or customers not on a free power period product would provide unfair cross subsidies to this cohort.

Forecast usage is uncertain

While products such as '3 for Free' are intended to be relatively simple for engaged customers, a free power product feature requires retailers to rely on complex assumptions around the forecast usage during the free usage window. This is because variable costs of supply continue to be incurred by retailers during this free period and must then be recovered through tariff components outside the free usage window for the product to be cost reflective.

There are significant challenges in determining the forecast cost of supply within the free usage window due to the variability of load shifting by different customer types, and the evolving nature of the energy transition including electrification of home and EV take-up rates.

For a regulated free power period product to be sustainable and efficient, the product would need to recognise these costs and reflect them in the tariff design. However, as noted previously, forecasting customer usage under free periods is innately difficult given the range of customer types that may take up such a product.

Without limitations on a free use product, this would inevitably mean that customer types with ordinary response capability would pay for benefits realised by customers with a greater response capability. In effect, this would also mean that customers who rent, do not own CER, or who are at work during the day, would likely pay for the benefits realised by customers who own a battery or EV or who are able to automate CER behaviour. We explore the safeguards that would be required to avoid this from occurring in the safeguard section below.

Even with safeguards in place there remains significant complexity in forecasting the usage patterns for the range of customers that would access such a product, particularly as the shift toward electrification progresses. It would be too early to confidently forecast representative customer load profiles that could forecast the cost of supply for a regulated free power period product price. Market insights and learnings are still required to inform the regulator and the industry on the appropriate forecasting methodology.

Free usage periods face three key variable cost drivers that must be reflected

As noted above, there are fundamental challenges in designing a regulated free power period tariff due to the variable costs of supply in the free usage window. Set out below are three key cost drivers that any free power period product framework must consider.

1. *The product must be based on a reasonable load-profile and Wholesale Energy Cost (WEC) calculations*

While zero or negative wholesale price events are an increasingly common feature in the wholesale market, the frequency and predictability of these events is not uniform. While spot market electricity prices in the middle of the day have in recent years been negative (or near zero) on many days, there are also many days where they are not. For example, less solar power is generated on cloudy days. Solar power generation also varies by other factors including season and region. The volatility of spot prices across different hours, days, seasons and regions are a risk that retailers must manage.

When averaged over the year, this will mean that wholesale energy costs (WEC) are unlikely to be zero for any proposed free usage period.

2. *A free power period is not supported by network tariffs*

A free electricity usage window every day on primary loads will also incur variable network costs based on the underlying network tariff. This is made more challenging by the varied network tariff structures available in each distribution zone. While Victorian DNSPs are proposing to introduce solar soak periods in their TOU tariffs, none of these tariffs have zero costs in the middle of the day. Further complications include the opt-in

application of export tariffs or rewards for CER customers. As with forecasting the WEC, the representative load profiles will again be a critical factor in estimating the variable network costs incurred during the free usage period.

These factors suggest that a TOU VDO would be a more efficient tariff to progress to encourage load shifting to take advantage of excess solar, rather than to progress with the complex development of yet another underlying network tariff, with zero costs, which would be inefficient.

3. The product must recover environmental scheme and AEMO costs

Environmental schemes including renewable energy targets and energy efficiency schemes such as the Victorian Energy Upgrades program create liabilities based on customer use. Substantial AEMO costs are also recovered on a usage basis. These costs are still incurred by use in a free power window and would need to be recovered through other components of the tariff.

Implementation of a free power period product must be doable

The availability of similar market retail products such as AGL and Ovo Energy's '3 for Free' product does not mean that it would be straightforward to launch a new, viable, regulated energy product with free power periods to market. These types of innovative offers are still very nascent in energy markets, and observations and lessons from their limited use are still actively being analysed by retailers before scaling them out further or making adjustments to broader offers.

The successful rollout of a free power period product would be predicated on retailers designing, developing and deploying new operational capabilities and customer collateral, as well as requiring retailers to design, build, test and deploy new customer communications, digital assets, and other marketing and educational materials.

Proposed information disclosure and consent requirements

There is a clear need to ensure that customers contemplating a product with a free power period have protections to ensure they are adequately aware of the features of the product and how best to benefit from it. This presents unique challenges if the product is a regulated standing offer, but one that may not suit the customer due to their specific circumstances.

We propose that a free power period product would need to be an opt-in only offer, requiring retailers to obtain explicit informed consent (EIC). However, we also note that The EIC framework under the Energy Retail Code (ERC) is established with market retail contracts in mind and does not necessarily translate or seamlessly apply to Standard Retail Contracts (SRC).

In many circumstances, consent is not needed to enter into an SRC, and there are several instances where it becomes the default arrangement between customer and retailer. Some caution should therefore be exercised in considering how a more complex regulated product could operate as a standing offer, when it may not be suitable for many types of customers, especially if they are not actively seeking to maximise potential value through load-shifting.

More broadly, the suitability of a regulated free power period product for any given customer may be challenging to assess, given in large part that is relies heavily on customer initiated behavioural changes.

Retailers may not have sufficient smart meter data to provide a wholesome assessment of the customer's load profile, and even if a retailer can assess the customer's existing load profile, it may not align to the beneficial time of use consumption behaviours for a free power product tariff. It is therefore inherently difficult to make product recommendations.

Reasonable safeguards must be established to protect all customers

Without robust safeguards, the implementation of a free power product risks shifting costs onto customers such as renters and non-solar and battery households. Enforceable safeguards are essential to protect equity and prevent cost blowouts.

Affordability must be a core principle of the development of a free power period framework. While standing offers are presented as a fair, trusted and reasonably priced electricity option, more complex products with free power periods but higher prices outside of this period may present challenges. This is because safeguards around consistency and comparability of offers are unlikely to protect consumers who have limited capacity to load shift during the day but are drawn to a message of affordability and equity.

Retailers offering comparable market products on the other hand, have some tools available to mitigate adverse impacts and unintended consequences such as fair use policies to prevent misuse and the ability to terminate the market retail offer and revert the customer onto an SRC.

Fair-use policy

Any free power period product should be complemented by a fair use policy to mitigate the risk of unfair and unequitable cross subsidies and avoid creating new network augmentation costs. A 'free' window is not cost reflective; it is below cost and therefore excess use within this window would create costs that must then be recovered within the VDO pricing framework or from other customers.

Applying safeguards to the free period is important to ensure that certain customer cohorts do not use the product in a way that disadvantages customers with limited ability to change their energy usage to access benefits from the free power period product. For example, battery and EV customers are more likely to be able to shift their consumption to greatly benefit from the free window. While this uptake of energy consumption is desirable to an extent, there is likely to be a threshold where excessive use will lead to unintended consequences.

For example, a homeowner with an EV and a large home battery could draw all their daily load in the free period, creating real usage (network) costs that would need to be recovered from other customers who may lack access to CER technology, thereby undermining the product's intent to promote equitable access to low-cost energy. This incentive to draw very large power loads over the free period can also reduce voltage outside of network limits, impacting customer experience, and leading to costly network augmentation, increasing electricity prices for all customers.

Excessive use would undermine the Victorian Government's broader objectives by creating unintended consequences such as increased wholesale prices during the free window, higher network voltages, and by leading battery customers away from orchestration products.

Safeguards could take the form of usage blocks, where consumption after a certain threshold would incur additional charges, or system size limits (kW or kWh) for certain devices. Customers could also be shifted to a default offer with no free period if persistent and excessive usage occurs. AGL has implemented a similar protection policy under its '3 for Free' plan, where the product can be terminated and a customer is shifted to an SRC if excessive use is detected.

Ensuring Informed Consumer Participation and Protecting Vulnerable Cohorts

The structure of regulated offers and the VDO suggests a level of protection to customers from higher prices, which may be appealing for vulnerable customers who are attracted to the presentation of a regulated tariff as including a period of free use. However, in the case of free power period products, customer value may rely heavily on customers actively seeking to shift their load into a free power period, and understanding the difference between costs incurred within the free period and in other periods. This requires customers to be well informed of the features of the product and how best to benefit from it, which may present unique challenges if the product is a regulated standing offer that a customer may access by default.

It is reasonable to expect that many consumers will be intrinsically drawn to a government-backed promise of 'free electricity'. Some of these customers may choose to access a free power period product even where, at best, they are unlikely to realise any material benefits from the free usage window or, at worst, could be disadvantaged by the generally higher prices associated with SRCs compared to other available market offers.

In the majority of circumstances, we expect that consumers will continue to be better suited to other traditional market contracts. Leaving this critical messaging to industry to navigate while positioning a free power period product as a solution to affordability issues for Victorians creates further risks of harm for some of the most vulnerable and disadvantaged cohorts.

If these customers remain on a standing offer and subsequently do not engage from the retail market, as commonly occurs with vulnerable customers, it becomes extremely difficult to re-establish meaningful contact, provide hardship support, move them off the standing offer and onto a more suitable market offer, and ensure that concessions and other payment support are correctly applied. Additionally, the Energy Retail Code of Practice will soon require retailers to automatically change customers' offers or prices in certain circumstances. The introduction of a free power period product into the mix of products that customers could conceivably be unilaterally switched to or from adds additional complexity and risk for both retailers and consumers alike.