

Industry-led electricity contract co-design

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Justice and Equity Centre
ABN 77 002 773 524
www.jec.org.au

Gadigal Country
Level 5, 175 Liverpool St
Sydney NSW 2000
Phone + 61 2 8898 6500
Email contact@jec.org.au



About the Justice and Equity Centre

The Justice and Equity Centre stands for a society that is fair and free from discrimination and disadvantage. Established in 1982 as the Public Interest Advocacy Centre (PIAC), we use the law and policy advocacy to challenge injustice and inequality. We do this through:

- legal advice and representation, specialising in test cases and strategic casework;
- research, analysis and policy development; and
- advocacy for systems change to deliver social justice.

Energy and Water Justice

Our Energy and Water Justice work improves regulation and policy so all people can access the sustainable, dependable and affordable energy and water they need. We ensure consumer protections improve equity and limit disadvantage and support communities to play a meaningful role in decision-making. We help to accelerate a transition away from fossil fuels that also improves outcomes for people. We work collaboratively with community and consumer groups across the country, and our work receives input from a community-based reference group whose members include:

- Affiliated Residential Park Residents Association NSW;
- Anglicare;
- Combined Pensioners and Superannuants Association of NSW;
- Energy and Water Ombudsman NSW;
- Ethnic Communities Council NSW;
- Financial Counsellors Association of NSW;
- NSW Council of Social Service;
- Physical Disability Council of NSW;
- St Vincent de Paul Society of NSW;
- Salvation Army;
- Tenants Union NSW; and
- The Sydney Alliance.

Contact

Michael Lynch, PhD
The Justice and Equity Centre
Gadigal Country
Level 5, 175 Liverpool St
Sydney NSW 2000

T: +61 2 8898 6500

E: mlynch@jec.org.au

Website: www.jec.org.au

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Recommendations

Selection Criteria

We recommend that an additional criterion is added to the existing selection criteria that explicitly references the NEO.

Modelling

We recommend that modelling of the implications of different contract design choices includes analysis of the performances of design choices under a set of energy market conditions that is very different to the current conditions.

We recommend that modelling of the implications of different volumes and tempos of contracting by the ESEM Administrator is included in the analysis of prospective contract design options.

Problem definition

We recommend that the co-design panel makes its recommendations concerning contract design options with a view not to resolving the shortfall between anticipated and needed supply of each energy service, but rather with a view only to removing the tenor gap impediment to investment in each energy service.

Defined role of ESEM contracts

We recommend that the role of ESEM firming contracts is limited to the management of events that can be efficiently priced by the market within the limits of the market price settings. This should not extend to rare events including dunkelflautes and kaltflautes.

We recommend that the proposed shaping ESEM contracts are extended to include inter- as well as intra-day shaping in line with the recommendations of the Nelson Report.

1. Introduction

The Justice and Equity Centre (JEC) welcomes the opportunity to provide a submission to AEMO Service Limited's (ASL) consultation paper on the industry-led electricity contract design (the consultation paper).

Consumer interests must be explicitly considered

While consumer stakeholders have not played a significant role in the design process to date, consumers carry some risks related to the contracts in question. As such the consumer interest should explicitly be included in the consideration of design alternatives.

Accordingly, we propose that the National Electricity Objective (NEO) is inserted into the selection criteria for the contract designs. Through this insertion, the implications of the contract design for consumers – outlined in this submission – should be given weight in the selection of design options for the three contract types.

In this submission we respond to a number of specific areas where consumer interest and risk to consumers should be a relevant consideration, and highlight the following:

- We recommend that the modelling of design options from this point onwards should include modelling the impacts of energy market conditions that are highly unlike today's conditions, even if such futures appear to be highly unlikely. This is an important aspect of appropriately considering risk to consumers.
- Electricity Service Entry Mechanism (ESEM) contracts are not intended to be the only tool to ensure adequate investment in bulk, shaping, and firming resources occurs. The co-design panel should not treat them as such. If it does, the effect will be to inefficiently shift risk and cost on to consumers and ultimately leave them paying more for their energy than they need to.
- We note that the effectiveness and systemic effects of the contracts will be materially impacted by the volume and depth at which the ESEM Administrator buys and sells each contract type. While this is not a design issue, the modelling work on the contract designs should include an interrogation of the impacts of different volumes and cadences of ESEM contracting, both to inform the ESEM Administrator's practice, and to identify weaknesses in any design options that emerge from this analysis.
- There is ambiguity concerning the length of outage that firming resources are intended to cover. We contend it is in consumers' interest that very rare outages that cannot be efficiently priced by the market are managed using out of market reserves alongside other mechanisms. Covering such events, including *dunkelflautes* and *kaltflautes*, should not be the intent of the ESEM firming contracts.

2. Risk held by consumers

Throughout the consultation paper there are references to the sellers and buyers of ESEM contracts. These are assumed to be generators in the former case, and either large users or retailers in the latter. This is slightly inaccurate. The second category should properly be referred to as 'eventual buyers'. The initial buyer of all ESEM contracts will be the ESEM administrator. The Administrator will hold each given contract from between 3 and 12 years, before identifying an eventual buyer. For the period the Administrator holds the contract, it is underwritten by consumers.

This does not mean that consumers are impacted by all the risk allocations occurring between the seller and eventual buyer of the contract. For example, as the Administrator never holds the contract during operational time, risks arising exclusively in operational time do not revert to consumers.

However, for the period that the Administrator holds each contract, consumers hold the risk that the given contract will retain its value and that an eventual buyer for it – at a reasonable price – will be found. This risk is bidirectional in that the price the Administrator receives for a given contract from the eventual buyer can be either lower or higher than the price the Administrator initially bought the contract for.

The most important thing for the consumer in this is that the contract retains value through time. In other words, the contract must be 'bankable' for both the seller (as the consultation paper notes) and the initial buyer, the ESEM Administrator.

This has implications for consumers which should be considered in finalising design options.

2.1 Inserting the NEO into the selection criteria

Given that consumers are impacted by the contract designs due to holding the initial buyer's bankability risk, their interests must be explicitly given weight in the consideration of design alternatives. This should be done by adding a further criterion to the existing criteria referencing the long-term interest of consumers or the NEO.

Recommendation 1: Selection Criteria

That an additional criterion is added to the existing selection criteria that explicitly references the NEO or the interests of consumers.

2.2 Modelling diverse energy market conditions

The 'bankability' of the contracts from the initial buyer/consumer's perspective is potentially jeopardised by the pace of change the energy system is experiencing and can reasonably be expected to continue into the foreseeable future. If the conditions are so dramatically different at the time the ESEM Administrator tries to sell a given contract that the price they receive has fallen substantially from the price they bought the contract at, this cost will be worn by consumers. Until that time the related risk is carried by consumers.

To manage this risk, we recommend that as part of options analysis for each of the three contract designs, sensitivity testing involving market conditions substantially different to the current ones should be added. The appearance of such conditions being very unlikely should not be considered a reason to discard sensitivities.

Sensitivities to test where dynamics differ to conditions forecast when contracts are agreed could include

- extremely low average spot prices over many months or years,
- extremely high average spot prices over many months or years,
- high spot price volatility, including sustained very low (negative) and very high prices,
- a high proportion of spot market settlements resulting in negative prices and high rates of economic curtailment,
- very high costs for storage, relative to the expected, and
- very high constraint rates for generators relative to the expected.

Recommendation 2: Modelling

That modelling of the implications of different contract design choices includes analysis of the performances of design choices under a set of energy market conditions that are very different to the current conditions.

3. ESEM contracts are not the only investment signal

There is a risk that the co-design panel undertakes their task as if the ESEM contracts are the only investment signals in the market, or the only tool responsible for avoiding a shortfall between anticipated and required generation providing each energy service. This would be problematic for two reasons.

- There are many other mechanisms that provide investment signals and incentives for energy resource providers to enter and remain in the market. These include spot prices themselves, the Electricity Statement of Opportunity among other publications from the Australian Energy Market Operator, and the jurisdictional investment underwriting offerings, such as the Long-Term Energy Service Agreements (LTESA) in NSW, which are expected to continue alongside the ESEM contracts.
- The ESEM contracts are designed to overcome the tenor gap, which is presented as a key impediment to market entry for prospective energy service providers. While this is a valid purpose, the tenor gap is not the only impediment to market entry reported by investors. The Clean Energy Outlook Report 2026 from the Clean Energy Investor Group lists the tenor gap as merely one of the key challenges facing prospective investors, ranking it behind 'Transmission buildout delays', 'Planning approvals', 'Grid connection

process and curtailment / negative pricing’ and ‘Access to grid and congestion’ in terms of importance.¹

Designing the ESEM contracts with a view to resolving entirely the shortfall between anticipated and needed supply would have two effects. The effort would fail as the ESEM contracts have no ability to resolve some of the noted impediments preventing investors from entering the market. It would also result in skewing the balance between making projects bankable for suppliers of energy and transferring risk and cost to buyers of energy. It would risk overcompensating suppliers of energy through inefficient costs being born by consumers.

Recommendation 3: Problem definition

That the co-design panel makes its recommendations concerning contract design options with a view only to removing the tenor gap impediment to investment in each energy service – rather than attempting to completely resolve the shortfall between anticipated and needed supply of each energy service.

4. Issues relating to the administration of the contracts

The volume and pace at which the ESEM Administrator buys and sells each type of contract will play a major role in shaping the initial buyer’s bankability risk held by consumers.

While the design of the contract cannot manage this risk or the role of administration dynamics, we recommend that the modelling of various contract design options includes examination of the impacts of different volumes and tempos of contracting.

Recommendation 4: Modelling

That modelling of the implications of different volumes and tempos of contracting by the ESEM Administrator is included in the analysis of prospective contract design options.

5. The appropriate role of each contract

5.1 Firming

The consultation paper is not clear on the role of firming services envisaged for the firming contracts with respect to the length or depth of outage the ESEM Administrator should aim to manage using contracts in the ESEM framework. Any firming contract will be an in-market mechanism and therefore its possible total duration is limited by the market price settings.

It is in consumers’ interest that very rare outages – which cannot be efficiently priced by the market – are managed using out of market reserves alongside other mechanisms, such as

¹ Clean Energy Investor Group, July 2026, ‘Clean Energy Outlook 2026’, https://www.ceig.org.au/wp-content/uploads/2026/07/2026-Clean-Energy-Outlook-Report_CEIG-.pdf, slide 18.

directed demand response and involuntary load shedding. Covering such events, including *dunkelflautes* and *kaltflautes*, should not be the intent of the ESEM firming contracts.

Recommendation 5: Defined role of ESEM contracts

That the role of ESEM firming contracts is limited to the management of events able to be efficiently priced by the market within the limits of the market price settings. This should not extend to rare events including ‘dunkelflautes’ and ‘kaltflautes’.

5.2 Shaping

The preferred shaping contract options identified by the panel appear to be limited to use for intra-day shaping. We note that this is not aligned with the recommendations of the Nelson Report – that shaping contracts be used for “[m]atching the intraday and inter-day profiles of supply and demand to meet regular peaks.”²

We recommend that work is done to align the proposed shaping contract with this mandate.

Recommendation 6: Defined role of ESEM contracts

That the proposed shaping ESEM contracts are extended to include inter- as well as intra-day shaping in line with the recommendations of the Nelson Report.

6. Further engagement

We welcome the opportunity to meet with the ASL project team, the co-design panel, and other stakeholders to discuss these issues in more depth. Please contact Michael Lynch at mlynch@jec.org.au regarding any further inquiries.

² Nelson, T. et al. (December 2025) ‘National Electricity Market wholesale market settings review; Final Report’. <https://www.energy.gov.au/sites/default/files/2025-12/national-electricity-market-wholesale-market-settings-review-final-report.pdf>, p.63.