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MDAG Chair
c/- Electricity Authority
P O Box 10041
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By email: mdag@ea.govt.nz

Dear James,

Re: Customer acquisition, saves and win-backs – Draft issues paper

Thank you for the opportunity to submit on the question of whether current "win-back" practices are to be considered an issue of market failure or what options retailers have to counter win-backs?

Pioneer Energy participates in the electricity market as both a generator and retailer. Our business is not a vertically integrated Gentailer in the normal use of the term, but each business operates independently as either generator or retailers. Two of Pioneer's businesses, Pulse Energy LP and Ecotricity LP operate as retail Limited Partnerships.

Customer satisfaction surveys clearly indicate that consumers are far less satisfied with the larger players than they are with a smaller retailer, so the only real issue with "win-backs" is whether the pricing being offered by larger players is fair and reasonable and reflects full market costs.

Our submission therefore primarily responds to Question 2 (ii)

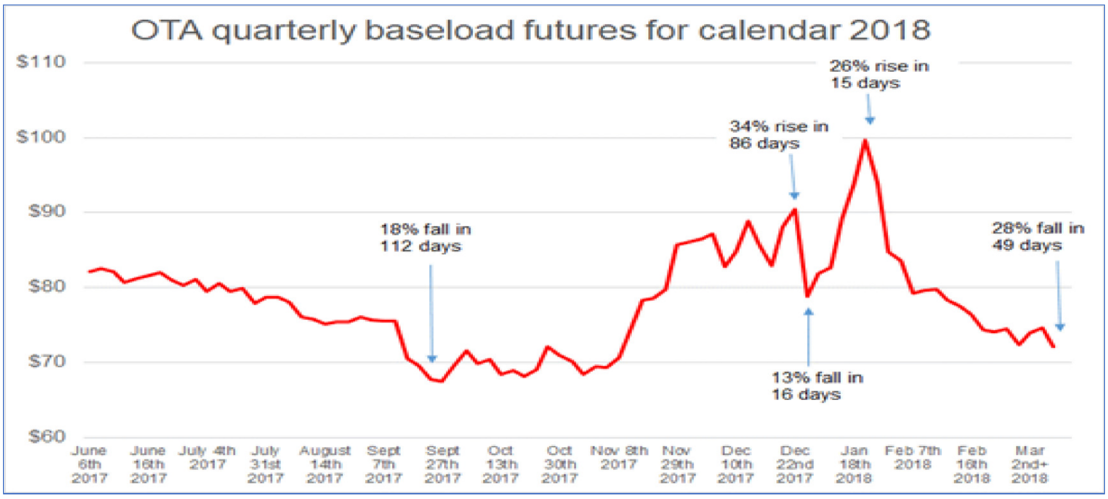
> *Is there any evidence that retailers have engaged systematically in proscribed marketing behaviours?*

Our view is YES, there are proscribed behaviours but these are not specific in general to *retailers,* but more specifically to the subset of retailers that are *Gentailers.* In this context, the proscribed market behaviours are systemic to Gentailer retailers. This specific subset of retailers (i.e. a minority group of the overall retail market participants) are using their market powers to limit the market shares of the independent retailers that rely upon these same Gentailers for their wholesale market supply.

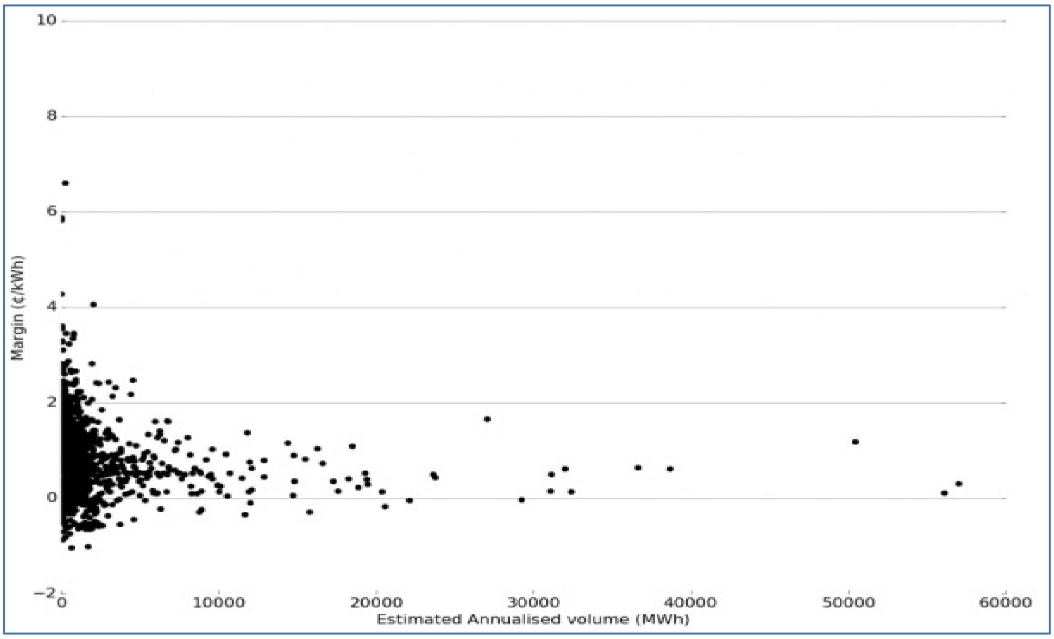
Use of Multiple Market Powers

The current "win-back" practices of Gentailers are just one of the compounding market performance issues the smaller independent retailers are facing in this market. The other market performance issues have been well signalled to the Electricity Authority (Authority) and industry stakeholders for some time, through numerous consultation processes and by direct complaints lodged with the Authority. These market performance issues include for example:

1. The wholesale futures market lacks sufficient liquidity to be used for retail supply risk management purposes – as evidenced by the recent unacceptable winter 2017 and summer 2018 price spreads. This is a critical issue for smaller retail investors.



2. Pricing practices in the FPVV tender market – where more than 12% of RFP tenders were found by the Authority to be priced below ASX wholesale prices in just one sample. We are disappointed that no further action has been taken – in MDAG's view what threshold constitutes systematic proscribed behaviours?



3. Prudential offsets between the wholesale and hedge contracting markets – a rejected market development opportunity as the Authority found modest NPV benefits. This analysis ignores the benefits of enabling small retailers. Further, the NPV benefits for this initiative are at the same level as the Authority used to justify its own intervention into the ACOT/DGPP Code at considerable cost and wealth transfers from DG owners to network businesses and consumers – where is the decision materiality consistency?

4. Customer compensation scheme – which imposes regulated costs on independent retailers that are greater than their gross margins during a market supply cost risk event. Again the financial sustainability of smaller investors was totally ignored in the decision to continue this interventionist type of wealth transfer from small investors to consumers.

Add together each of these material risks to smaller and new entrant investors, and we have a market that is becoming unsustainable for the smaller businesses, whether generating or retailing. On this current market development trajectory, consumers will have less choice, face more draconian contracts and see limited innovation, directly as a consequence of the four market issues listed above.

Recommendations

We recommend MDAG takes a broader perspective on win-back behaviours by Gentailers and looks deeper for evidence into how the win-back pricing compares to the standard published terms. That is, do the discount margins offered for contracted terms on win-back customers fairly reflect the differences from posted standard terms? For example:

- With standard published terms retailers generally have the option to re-price the contracts annually or within a notice period – i.e. they carry one year of market price risk. Do the terms offered for "win-backs" reflect the ASX forward prices for the contracted term?

- How does the win-back discount margin compare to normalised acquisition/churn costs – of generally around $120 per residential customer. Do the pricing incentives offered reflect the market value of what is a price sensitive customer?

- Could that same on-the-switch "win-back" contract price, over the term offered, also be offered to all their retail consumers at a price reflective of generation investment costs and supply risks?

Our guess is many of the on-the-switch "win-back" prices would not fairly reflect Gentailer investment costs and supply risks. This very same issue was raised with the Authority in the FPVV tender market and their investigation showed more than 12% of FPVV term contracts were priced below the prevailing wholesale market hedge prices. As "win-back" prices make up about 12% of all retail market prices, our question is whether these same market pricing behaviours are also happening in the most contestable segment of the mass market?

If it proves to be so, then more than 12% of the retail market is being priced below wholesale and risk costs, which is at the level of trade switches in the market. i.e. there is no room for new retail entrants without also having new generation.

In our view, only the Authority and Commerce Commission have the regulatory powers to do this investigation thoroughly in terms of having market evidence. We therefore recommend that MDAG requests the Authority undertake the same market investigation as they did for the FPVV contract market on the recent NHH "win-back" contract prices. That is, to review the actual prices made on the "win-back" deals and contract terms and then compare these prices to the market posted retail prices. Only then will we have sufficient real evidence to determine whether the combination of FPVV tendered and NHH metered "win-back" prices are fair and there is reasonable competition.

We appreciate the opportunity to submit on these important matters for smaller market investors such as Pioneer and its partner retail businesses.

Yours truly

Fraser Jonker
Chief Executive