July 9, 2018

James Moulder
MDAG Chair

Re: Save Protection Scheme Response from Pulse – Save Protection Scheme

James,

Please accept this letter as Pulse's response to your request of views on the current Save Protection Scheme. It is supplemental to other views expressed to the EA and MDAG previously and should be read as additional points of view from Pulse on the matter.

The Scheme should be analysed based on how it can be manipulated

In our view, to fully understand the faults of the current Save Protection Scheme, it must be examined through the eyes of a dominant retailer with substantial market share to protect. Based on statistical circumstances and observed market behaviour, Gentailers are more likely to use the scheme as a strategy to retain a customer and challenging retailers are the participants who are more inclined to invest in acquiring new customers by luring them away from a Gentailer.

In this regard, the current scheme enables poor market behaviour and the leveraging of required market processes such as switching, by protective retailers in a number of ways.

These are:

1) **Protection based strategies minimise acquisition costs and reduce consumer benefit**

Gentailers, keenly focused on maintaining their market share, can adopt a strategy where a recently departed customer can receive special accommodations that they are not inclined to offer their entire customer base, so as to maximise profits.

When Gentailers are notified of a switch, they can instruct their save team to recover the lost customer at any cost. Even if the resulting delivered retail price substantially undercuts the wholesale price, it would worthwhile as they can rationalise that less margin on this customer is a minor cost if it serves to communicate to the challenging retailer that they should seek customer's elsewhere and avoids the need to reduce prices in general. The long-term effect of this is to deter challengers from competing with their brand when encountered.

In short, losing money on 1% of the customers is far better than lowering prices across the entire customer list and deterring competition leads to long-term profit-maximisation. This equation for maintaining market share is far less expensive than acquiring new customers and, as a consequence, minimises the consumer benefits at the same time.

2) Early win-backs reduce competition through unwanted lock-in periods

In addition to undercutting the wholesale price, Gentailers can include other devices to induce recovery of a lost customer, such as adding a cash credit that is redeemable at the end of a long lock-in period (or refundable in the form of a larger termination fee).

This mechanism is probably more effective than undercutting the wholesale price as it "sounds attractive" in a marketing sense and will take this particular customer off the market for a significant period of time.

These customers lose any freedom to seek better offers and the challenger retailer receives no compensation for the cost and effort of bringing a lower priced option to this customer in the first place. The losing retailer retains a customer instead of investing in acquiring a new one. In this regard, the losing retailer free-rides on the investment of the challenger brand and reduces the quantity customers free to choose should better prices arise in the future.

3) Leveraging the "heat-of-the-moment" reduces consumer benefits and unfairly taxes a challenger retailer

As it currently stands, the scheme facilitates and endorses the process of leveraging the "heat-of-the-moment." The short duration of time between when a switch is completed and when a win-back call is executed is critical to the success of an early win-back.

Literally within minutes of getting a switch notification, Gentailers are free to tells the customer that there is no reason to be concerned about unwinding the deal they made with the gaining retailer. For consumers who honour commitments, "unwinding" is easier to accept than "cancelling a deal they just made".

The "heat of the moment" often includes a "better act now" warning from the win-back agent. This adds urgency pressure that is likely false – but to a customer, heard as if a fact.

The consequence of this is the "heat of the moment" leverage allows a Gentailer to offer less than they would otherwise. For example, if a losing retailer was forced to wait 60 days before they could encourage a customer to return, they may be forced to offer a better price and/or a larger credit as the urgent pressure is removed.

The resulting impact is the challenging retailer writes off the sales costs and the consumer is pressured into doing something they might otherwise choose not to do; particularly if it includes a locked-in period as referred to in 2) above.

4) Gentailers can engineer "no-fly zones"

A consequence of enabling early win-back strategies is Gentailers can create "no-fly zones".

If a challenging retailer is effective in a region, Gentailers can use early win-backs to shut them out completely. It would not take too many time periods where Gentailers win-back 100% of the sales to cause the challenger to move on to another place or chose another strategy. If sustained, Gentailers may even be able to put them out of business.

If all Gentailers are successful in setting up no-fly zones, the market ceases to function and challenger competition grinds to a halt.

5) Door-to-door sales can be effectively closed out

Challenger retailers often use door-to-door sales as a means of acquiring customers and early win-backs can make this process uneconomic.

It is very easy for a Gentailer to detect when a door-to-door campaign begins as they will notice a pattern of switches down to the level of which street the door to door sales people are working. This creates an opportunity to enact special win-back scripting to overcome the encroaching retailer's activity.

This scripting can be tailored to disparage the retailer's message or pitch. It can cast doubt about the long-term sustainability of an upstart retailer. This opportunity is nearly impossible to achieve in any other way as the one-on-one "heat of the moment" can be very specific and very personalised. It goes without saying that general and open disparagement of a retailer would not be acceptable in a fair-trading context.

Since most door-to-door sales people are on a commission structure, sending them the message that they will not be successful in a particular street or area will cause them to go somewhere else and hopefully only invest time in another retailer's customer.

There is no reason why a channel used to gain a customer should affect the likelihood of that customer being regained by their former retailer. This is evidence of a market failure.

6) Gentailers can use the win-back process to cherry-pick

Gentailers can use the early win-back process to cherry pick and retain their best customers. Keeping large users and ones with low credit risk are clearly more desirable and these customers tend to be apathetic by nature.

The Save protection scheme enables cherry-picking as protection-oriented retailers can sit back and wait for a good margin customer to act before doing anything for them; and let less profitable ones freely go.

The structure of the current Save Protection Scheme has fundamental problems

These are:

1) A Save and a Win-back are the same thing and are both redundant

The use of the mandated switch process as the trigger for a win-back and for drawing distinction from a save has achieved nothing other than speeding up switching and continuing to facilitate customer price discrimination.

As a result, it is now clear that a save and a win-back have become the same thing. Furthermore, the concept of a "save" or a "win-back" is not even a required set of market terminology.

If a consumer chooses a new retailer, and the market rules allow for the transaction to be completed, then the only remaining market activity is the losing retailer makes a new offer to lure them back. Retaining the concept of a "save" is not helpful or needed if regulation prohibits interference in the challenging retailers acquisition and encourages competition on a level playing field.

2) The Scheme's Opt-in provision is inherently faulty

"Opting-in" to a mechanism that creates a level playing field is, in itself, a self-defeating mechanism. It can be misconstrued by a customer as their new provider is "against competition" and opting-in for protection can be used by a losing retailer as incriminating evidence of that.

Regulation that directly or indirectly indicates that a challenging retailer may need or want protection from a competitor is an indication of a market design flaw or a market failure.

It is far more robust to have all rules mandatory and all players a participant in creating a level playing field. The scheme needs to be changed and made mandatory; regardless of whether or not the participant is "protectionist" or "challenging".

3) A win-back is an Unsolicited Offer that is not declared so

One of the realities of soliciting a new customer is there are several consumer protections that need to be explained before they are bound by the offer. The requirement to explain these protections to a new customer, while a good idea, is meant to trigger caution in a customer's decision-making process.

Because of this trigger, it is far easier to interfere with that decision in an early win-back call than to convince them to switch in the first place.

Ironically, allowing these explanations to be by-passed in an early win-back call removes the trigger of caution that was intended in the first place. In other words, the challenger faces a constraint the win-back retailer does not; indicating a market failure or an un-level playing field.

4) The Scheme operates as if the losing retailer has a last-right-of-refusal

We do not believe a fair market should allow contracts to include a last-right-of-refusal and if the idea was proposed, we believe it would be rejected by regulators. Allowing the Save Protection Scheme to operate in this way, enables actions and strategies that would otherwise be unacceptable.

We believe for this reason alone, the activity should face strict prohibition.

Solutions

We believe the solution is easy to implement. The way to comprehensively fix these problems to is to:

1) The simple way to put fair pressure on protection-based strategies would be to insert a prohibition period of 60 days before a counter-offer is possible. This would ensure the highest counter-offer is made and allow the challenger retailer an opportunity to establish a relationship with their new customer. The customer will also have time to consider other options at that time which may or may not include a lock-in period;

2) Make all participation in the regulation mandatory. All retailers should be on on a level playing field, so “opting-in” is an illogical construct; and

3) Remove the concepts of “saves” and “win-backs” completely - as competition should be a simple process of offers and counter-offers. Inserting a 60-day period before a counter-offer is all that matters. All unsolicited offers are treated equally and switching should be open and equitable. A customer commitment can only be “unwound” by a fairly positioned offer by another player; whether or not that player once served that same customer.

Conclusion

In conclusion, we feel discouraging challenger retailers and repeatedly unwinding their offers will have a long term detrimental impact on their sustainability and consequently is not for the long term benefit of consumers. Using high pressure sales in the “heat of the moment” reduces consumer benefits and can invoke consent for an offer they might not otherwise want.

Allowing protectionist Gentailers to use the scheme to target retailers, cherry-pic customers, and lower acquisition costs is not fair competition. Consumer interests will not be served if challengers disappear or no-fly zones are created. The scheme does not promote competition in the electricity industry, in fact it facilitates price discrimination by incumbents.

At Pulse, we believe the market is best served when challengers can thrive, consumers can switch easily with no-cost termination options and Gentailers earn a replacement customer on a level-playing field. Our view is consistent with the Authority’s statutory objective.