

Barriers to group switching and mass market aggregation

Report by the Retail Advisory Group

10 September 2014

Contents

1	The RAG has reviewed barriers to group switching and mass market aggregation	2
2	Summary of the RAG’s conclusions regarding group switching and mass market aggregation	2
3	The RAG’s recommendation regarding group switching and mass market aggregation	3
4	The RAG has given the issue proper consideration and followed a consultative process	3
5	What problem has the RAG investigated?	4
6	The RAG has looked at potential benefits from, and limitations to, group switching and mass market aggregation	4
6.2	Preliminary results of the RAG’s review	5
6.3	The RAG’s preliminary thoughts on possible actions the Authority might take to improve group switching and mass market aggregation	5
7	Feedback from the RAG’s consultation with interested parties	6
8	The RAG’s findings from its review of group switching and mass market aggregation	8
8.2	Group switching and mass market aggregation exist, and provide benefits to some consumer groups	8
8.3	There is no conclusive evidence about the scale and materiality of benefits from increases in group switching and mass market aggregation	8
8.4	The RAG has not identified any barriers to group switching and mass market aggregation	9
8.5	The Authority is already addressing several hurdles to group switching and mass market aggregation	9
8.6	The Authority could assist the understanding and awareness of consumers and buying groups / aggregation schemes	10
8.7	The Authority should not intervene in one area – consumer credit history	11
	Appendix A Potential limiting factors to group switching and mass market aggregation consulted on by the RAG	12

Appendix B Potential benefits from group switching and mass market aggregation	14
---	-----------

Appendix C Key comments and themes in formal submissions on the RAG's discussion paper	17
---	-----------

Tables

Table 1	Formal submissions on group switching and mass market aggregation discussion paper	6
Table 2	Summary of potential limiting factors to buying groups and mass market aggregation	12

Retail Advisory Group

Membership of the Retail Advisory Group (RAG) changes from time to time, as members resign, members' terms expire and new members are appointed. This paper is approved by the members of the RAG as at 10 September 2014. The members of RAG are:

Peter Allport (Chair)

Ewan Gebbie

Sue Chetwin

James Munro

Nathan Strong

Alan McCauley

Allen Davies

James Tipping

Nick Robinson.

Previous RAG members that contributed to this paper are:

Dene Biddlecombe

Andrew McLeod

Sarah Free.

1 The RAG has reviewed barriers to group switching and mass market aggregation

- 1.1.1 The Retail Advisory Group (RAG) provides independent advice to the Electricity Authority (Authority) on the development of the Electricity Industry Participation Code 2010 (Code) and market facilitation measures, focusing on the relationships between retailers, distributors and consumers.
- 1.1.2 In August 2013 the Authority asked the RAG to undertake a review of barriers to group switching¹ and mass market aggregation² in the New Zealand electricity market. The purpose of the review was to examine the benefits of electricity consumers establishing or joining buying groups / aggregation schemes, and to investigate whether there are barriers inhibiting group switching.
- 1.1.3 In particular, the RAG was requested to examine:
 - a) the opportunities for, and potential benefits of, household or small business consumers aggregating to negotiate terms and conditions with electricity suppliers that are more favourable than each consumer could achieve individually
 - b) whether there are factors limiting group switching and whether there are factors discouraging retailers from engaging with buying groups
 - c) whether there is anything the Authority can or should do to remove barriers to group switching.
- 1.1.4 The RAG has now completed its review. This report contains the RAG's recommendation to the Authority.

2 Summary of the RAG's conclusions regarding group switching and mass market aggregation

- 2.1.1 The RAG has reached the following conclusions about group switching and mass market aggregation in New Zealand:
 - a) group switching and mass market aggregation activities exist and provide benefits to some electricity consumer groups
 - b) there is no conclusive evidence about the scale and materiality of benefits from increases in group switching and mass market aggregation
 - c) the RAG has not identified any barriers to group switching and mass market aggregation activities

¹ Group switching is defined as a group of consumers, who have got together to negotiate a group deal with their electricity retailer, switching retailer at the same time.

² Mass market aggregation is defined as the act of grouping consumers together to negotiate a group deal with their electricity retailer. Often a third party acts as the aggregator.

- d) the Authority is already addressing several hurdles to group switching and mass market aggregation
- e) the Authority could assist the understanding and awareness of consumers and buying groups / aggregation schemes
- f) the Authority should not intervene in one area – consumer credit history.

3 The RAG's recommendation regarding group switching and mass market aggregation

- 3.1.1 The RAG recommends the Authority take no specific action in respect of group switching and mass market aggregation in New Zealand, but continue addressing general barriers to consumer switching.

4 The RAG has given the issue proper consideration and followed a consultative process

- 4.1.1 The RAG began its review of barriers to group switching and mass market aggregation in October 2013. The review consisted of the following steps:
- a) the RAG prepared a discussion paper on issues relating to group switching and mass market aggregation in the New Zealand electricity market. This work was undertaken between October 2013 and March 2014
 - b) the RAG consulted with interested parties on the issues identified in its discussion paper.³ Consultation occurred in April and May 2014
 - c) at its 11 June 2014 meeting the RAG considered the eight submissions received on the discussion paper.⁴ The RAG expressed concern that feedback on the discussion paper was not from a sufficient cross section of interested parties to gather reliable feedback on the recommendations. The RAG requested its secretariat seek feedback on the discussion paper from consumer groups and buying groups
 - d) in July 2014 the RAG secretariat contacted a further 13 potentially interested parties from consumer groups and buying groups, to seek their feedback on the issues raised in the discussion paper. Four parties responded and three provided informal feedback on the discussion paper and the conclusions reached within it
 - e) at its 10 September 2014 meeting the RAG finalised its recommendation to the Authority regarding barriers to group switching and mass market aggregation.

³ Retail Advisory Group, Barriers to groups switching and mass market aggregation discussion paper, available at, <http://www.ea.govt.nz/development/work-programme/retail/group-switching/consultations/#c12196>.

⁴ Submissions and summary of submissions, Barriers to groups switching and mass market aggregation discussion paper, available at, <http://www.ea.govt.nz/development/work-programme/retail/group-switching/consultations/#c12196> and <http://www.ea.govt.nz/development/advisory-technical-groups/rag/meeting-papers/2014/11-june/>.

5 What problem has the RAG investigated?

5.1.1 The RAG has developed the following problem definition for the current situation with group switching and mass market aggregation:

“There are limited group switching and mass market aggregation activities in the New Zealand electricity market, relative to other sectors. This inhibits consumer participation in the retail electricity market, which reduces the achievable long-term benefits to consumers”.

5.1.2 Investigations during the development of the discussion paper, and feedback from submissions on it, suggest this situation is primarily caused by:

- a) relatively high transaction costs and small margins associated with aggregating mass market electricity consumers, relative to mass market consumers in other sectors
- b) electricity consumers not being sufficiently aware of the options available to them in respect of group switching and mass market aggregation, and the potential benefits from being part of a buying group
- c) a lack of mass market electricity consumer groupings that are suitable for simple and effective aggregation
- d) difficulties establishing an attractive value proposition from mass market aggregation for consumers, suppliers and potential providers of group switching services.

6 The RAG has looked at potential benefits from, and limitations to, group switching and mass market aggregation

6.1.1 The RAG’s discussion paper canvassed the following five areas:

- a) background information on group switching and mass market aggregation, including examples of group switching in New Zealand and internationally
- b) the scale and extent of opportunities and potential benefits that could be expected to arise from group switching and mass market aggregation
- c) factors limiting group switching and mass market aggregation, and whether any of these are genuine regulatory barriers that could be resolved by regulatory intervention
- d) preliminary results from the RAG’s investigation and identification of potential benefits from addressing the identified limitations on group switching and mass market aggregation
- e) the RAG’s preliminary thoughts on actions the Authority might undertake to improve group switching and mass market aggregation in the New Zealand electricity market.⁵

⁵ For further detail on any of the five areas, please refer to <http://www.ea.govt.nz/development/work-programme/retail/group-switching/consultations/#c12196>.

6.2 Preliminary results of the RAG's review

- 6.2.1 The main conclusion reached by the RAG in its discussion paper was that there are a number of potential or actual hurdles to the effective formation of buying groups. Appendix A contains a summary of the 11 hurdles identified by the RAG. However, the RAG did not identify any barriers preventing the formation of buying groups.
- 6.2.2 The RAG identified some market/regulatory arrangements that could be made more effective to better enable the emergence of buying groups. However, whilst improving these arrangements might lead to more group switching, they are not critical to its existence.
- 6.2.3 To a large degree, buying groups face the same hurdles to aggregating electricity customers as do new entrant retailers. These should be seen as part of the normal cost of participating in the retail electricity market. The RAG considered that it was outside the Authority's functions and powers to seek to remove or suppress commercial realities facing providers of group switching services.

6.3 The RAG's preliminary thoughts on possible actions the Authority might take to improve group switching and mass market aggregation

- 6.3.1 In the discussion paper the RAG identified the following areas of further work or Authority intervention as being worthy of consideration:
 - a) examining further the existence of genuine regulatory barriers to forming buying groups, including provisions in the Code, and developing Code amendments to resolve any barriers found in the Code
 - b) developing further the models and quantification work set out in the discussion paper,⁶ with a view to providing a greater level of insight into the scope and extent of the opportunity presented by group switching and mass market aggregation
 - c) improving access to retail consumer information either as part of the retail data project or in addition to it
 - d) producing information intended to act as guidance for parties interested in forming buying groups, including the factors likely to promote success, and an understanding of the economics involved
 - e) putting in place a public information/education campaign (equivalent to the "What's my Number?" campaign) that outlines the existence of electricity buying groups and the potential benefits from joining them
 - f) undertaking reviews of, and changes to, the switching process and registry structure.
- 6.3.2 The RAG concluded that the most substantive interventions the Authority could reasonably undertake were already within the scope of the Authority's retail data project. Indirect regulatory activity such as promotional and educational activities in respect of

⁶ Refer to Appendix B for further detail.

group switching and mass market aggregation should be considered on their own merits and pursued accordingly.

7 Feedback from the RAG's consultation with interested parties

7.1.1 Eight formal submissions were received on the RAG's discussion paper. These are listed in Table 1.

Table 1 Formal submissions on group switching and mass market aggregation discussion paper

Retailers/Generators	Networks	Other
Contact Energy Genesis Energy Meridian Energy Mighty River Power Nova Energy TrustPower	Powerco	Electricity & Gas Complaints Commissioner

Source: Retail Advisory Group, Review of barriers to group switching and mass-market aggregation, Summary of submissions, 11 June 2014, p.2.

7.1.2 The RAG requested additional targeted consultation be undertaken after concluding that the submissions did not adequately represent the views of (residential) consumer groups or proponents of buying groups. Informal feedback was received from three of 13 parties contacted by the RAG secretariat.

7.1.3 The key comments and themes contained in formal submissions on the RAG's discussion paper can be grouped into four areas:

- a) experience with electricity buying groups in New Zealand
- b) feedback on the size of the potential benefits from group switching and mass market aggregation
- c) potential limiting factors for group switching and mass market aggregation
- d) submitters' views on the RAG's conclusions and recommendations.

7.1.4 Submitters' views on the RAG's conclusions and recommendations can be summarised as follows:⁷

- a) four submitters⁸ agreed with the RAG's recommendation that the Authority should complete the retail data project

⁷ Refer to Appendix C for a summary of views from formal submissions on the first three areas listed above.

⁸ Contact Energy, Genesis Energy, Powerco and TrustPower.

- b) three submitters⁹ believed no further investigation of group switching and mass market aggregation was warranted, or should be undertaken by the Authority
- c) three submitters¹⁰ submitted that no specific additional actions were required
- d) no submitters suggested additional or alternative actions that should be taken by the Authority in relation to group switching and mass market aggregation
- e) two submitters¹¹ believed it was inappropriate for the Authority to assign resources to supporting for-profit business models
- f) one submitter¹² considered that any promotional work initiated by the Authority should be aimed at helping electricity consumers understand the benefits of switching and how this works with buying groups, while another submitter¹³ did not agree with the Authority considering any promotional or educational activities about group switching and mass market aggregation
- g) two submitters¹⁴ agreed with the RAG's conclusion that the Low Fixed Charge Regulations present a barrier to flexibility and innovation
- h) one submitter¹⁵ believed that the Authority's future work to encourage switching should be focused on promoting the benefits of switching and resolving the post-Part 10 implementation switching and registry issues.

7.1.5 The views of the three submitters who provided informal feedback to the RAG can be summarised as follows:

- a) one party contacted in relation to potential brokerage models for electricity agreed a brokerage model may be relevant, but was unable to add any further information regarding electricity, except that it was unlikely mortgage or insurance brokers would be interested in brokering electricity. The party also provided a link to a cautionary article that implies brokerage fees paid for switching in overseas jurisdictions may actually work against the long term benefit of consumers
- b) one party contacted based on its involvement with rural group buying offerings commented that the value proposition to and from farmers is quite different to that for residential consumers, in that on-farm electricity use is a substantial component of a farmer's business cost. Additional benefits accrue from credit management and combined invoicing. The party was sceptical that similar benefits would exist for residential consumers
- c) one party involved with brokering energy procurement commented that:

⁹ Contact Energy, Meridian Energy and TrustPower.

¹⁰ Contact Energy, Meridian Energy and Mighty River Power.

¹¹ Genesis Energy and Mighty River Power.

¹² Meridian Energy.

¹³ Mighty River Power.

¹⁴ Genesis Energy and Meridian Energy.

¹⁵ Meridian Energy.

- i) informational barriers such as access to consumption information, and the complexity of tariffs and charges, make the task of aggregating consumers more difficult
- ii) consumers are interested in both price and non-price features of an offering, which complicates the aggregation task further
- iii) the small-to-medium enterprise (SME) sector is poorly covered by service providers at present, and may be able to be aggregated effectively
- iv) some government agencies would seem to have customers that could be grouped effectively to provide benefits to consumers, suppliers and taxpayers
- v) aggregators are dependent on both consumers and suppliers to succeed, and as such may find it hard to provide impartial service to all parties
- vi) the value proposition to both consumers and suppliers is key to the success of the buying group
- vii) it can be virtually impossible to ensure that the grouped value proposition is equally attractive to all individuals within the group.

8 The RAG's findings from its review of group switching and mass market aggregation

8.1.1 Following its consideration of feedback from interested parties, the RAG has reached a number of conclusions.

8.2 Group switching and mass market aggregation exist, and provide benefits to some consumer groups

8.2.1 The RAG's review has found that group switching and mass market aggregation exist for some parts of New Zealand's electricity industry and are beneficial to the consumers, suppliers and aggregators involved. Examples include rural services companies in the farming sector, all-of-government procurement, and special interest groups.

8.2.2 Commercial and industrial electricity consumers appear to be relatively well served by energy brokers and energy services companies.

8.2.3 Mass market residential consumers and SME consumers do not appear to be well served by group buying schemes / aggregators.

8.3 There is no conclusive evidence about the scale and materiality of benefits from increases in group switching and mass market aggregation

8.3.1 The RAG considers that some potential benefits exist from increases in group switching and mass market aggregation (refer to Appendix B for a summary of these and to Appendix C for a summary of submissions on these). However, discussion within the RAG

and feedback from consultation clearly indicates there is no widespread agreement on the scale and materiality of these benefits.

- 8.3.2 The RAG has identified some possible approaches to expand the understanding of these potential benefits and to improve the veracity of the estimate of their size. However, the RAG does not recommend pursuing additional work in this area. The primary reason is that the RAG is of the opinion that the additional clarity obtained will not be sufficiently valuable to justify the effort required.

8.4 The RAG has not identified any barriers to group switching and mass market aggregation

- 8.4.1 As noted earlier, the RAG identified 11 potential or actual hurdles to the effective formation of buying groups in its discussion paper. These were grouped under two headings:

- a) General limiting factors
- b) Possible regulatory barriers.

- 8.4.2 The RAG identified three possible barriers to group switching and mass market aggregation that were regulatory in nature:

- a) the customer switching process in the Code may place limitations on group switching, thereby reducing the level of transaction cost savings available
- b) the structure of the registry may complicate the group switching process
- c) the Low Fixed Charge Regulations limit flexibility and innovation in group-switching offerings.

- 8.4.3 Following consideration of submissions, and consistent with its preliminary view in the discussion paper, the RAG has concluded these are not barriers to group switching and mass market aggregation per se. Instead, the RAG considers them to be hurdles, which are not relatively significant in nature.

- 8.4.4 The RAG notes it is considering two of these hurdles as part of its work programme (through its reviews of the customer switching process and the Low Fixed Charge Regulations). The RAG considers that any review of the registry should have the objective of ensuring the registry facilitates all aspects of the customer switching process, rather than just group switching.

8.5 The Authority is already addressing several hurdles to group switching and mass market aggregation

- 8.5.1 The discussion paper, and feedback on it, identified that a lack of information and the complexity of tariffs and retailers' offerings were key limiting factors to switching in general, and to group switching and mass market aggregation in particular.
- 8.5.2 Of the eight 'general limiting factors' to group switching and mass market aggregation identified in the discussion paper, the Authority is currently addressing three:

- a) customers are not engaged with the electricity purchasing decision (via initiatives under the consumer switching fund or its replacement)
- b) there is insufficient information about tariffs and metering configurations for buying groups to aggregate customers and find good deals (via the retail data project)
- c) there is insufficient information about consumer profiles and consumption data (via the retail data project).

8.5.3 The RAG recommends that the Authority continues to prioritise work to address general barriers to retail switching and competition that also impact on group switching and mass market aggregation, specifically:

- a) insufficient information for electricity consumers to easily make informed decisions about their choice of supplier
- b) complexity introduced by the Electricity (Low Fixed Charge Option for Domestic Users) Regulations 2004
- c) transparency of consumer charges, in particular distribution charges.

8.6 The Authority could assist the understanding and awareness of consumers and buying groups / aggregation schemes

8.6.1 A factor limiting the growth of group switching and mass market aggregation is insufficient consumer understanding and awareness of the potential benefits from participating in a buying group / aggregation scheme.

8.6.2 Another potential limiting factor is a lack of understanding, on the part of buying groups / aggregators, of what is needed to operate successfully. This includes understanding:

- a) the needs/requirements of electricity consumers and retailers
- b) establishment and operating costs
- c) regulatory/legal requirements.

8.6.3 Four of the eight 'general limiting factors' to group switching and mass market aggregation identified in the discussion paper relate to these matters:

- a) customers are not aware of buying groups and the potential benefits of involvement
- b) buying groups are not providing a strong value proposition to consumers
- c) buying groups are not providing a strong value proposition to retailers
- d) buying groups face strategic/tactical hurdles.

8.6.4 Following consideration of submissions, the RAG has concluded that the Authority could assist the understanding and awareness of consumers and buying groups by fulfilling an educational / information provision role (refer to examples from the United Kingdom).¹⁶

¹⁶ DECC collective purchasing and switching guide for consumers, available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/36699/5368-collective-purchasing--guidance-for-consumers.pdf: the guide states that its purpose is to give consumers some guidance on what to think about if they are

8.6.5 However, the RAG is uncertain whether educational and promotional activities intended to address these limiting factors will be cost-effective. Since the target audience for such activities is not known or readily identifiable, the RAG is concerned that the Authority may incur significant costs reaching the audience. As noted above, there is no widespread agreement on the scale and materiality of the benefits from group switching and mass market aggregation. Hence, the RAG is unsure of the net benefit from the Authority undertaking such activities. The RAG recommends these be subject to a cost-benefit assessment.

8.7 The Authority should not intervene in one area – consumer credit history

8.7.1 The final ‘general limiting factor’ to group switching and mass market aggregation identified by the RAG in its discussion paper was insufficient information about consumer credit history being available to buying groups and retailers.

8.7.2 The RAG considers this to be a commercial matter, and has concluded that the Authority should not take any specific action about this.

considering joining a collective purchasing and switching scheme; Collective switching guide for scheme organisers, available at: <https://www.gov.uk/government/publications/collective-switching-guidance-for-scheme-organisers>; this contains a collective switching guide for UK collective switching scheme organisers published by DECC. The executive summary of the guide states that its purpose is to give “scheme organisers such as local authorities, housing associations and charities, some guidance on what to think about before setting up a collective switching scheme and reflects best practice and feedback from previous schemes”; Ofgem, Open letter on collective purchasing and switching schemes, available at: <https://www.ofgem.gov.uk/ofgem-publications/38442/collective-switching-open-letter.pdf>

Appendix A Potential limiting factors to group switching and mass market aggregation consulted on by the RAG

A.1 The RAG consulted on various factors potentially limiting the growth and success of retail buying groups in New Zealand. Table 2 summarises the RAG's consideration of these in its discussion paper.

Table 2 Summary of potential limiting factors to buying groups and mass market aggregation

No.	Limiting factor	Impact	Potential solutions	New/existing Authority work
	<i>General limiting factors</i>			
1	Consumers not engaged with electricity purchasing decision	Buying groups struggle to acquire customers, meaning customers miss out on savings	General promotion of the benefits of switching	Existing: Consumer Switching Fund or any replacement of it. No specific intervention for group switching
2	Consumers not aware of buying groups and potential benefits of involvement	Buying groups struggle to acquire customers	Promote understanding of how buying groups work and the benefits available	New: Fact sheets and explanatory material about buying groups. Website listing active groups and key features
3	Insufficient information about tariffs and metering configurations for buying groups to aggregate consumers and find good deals	Buying group offerings will be either overly generic or overly consumer-specific, both of which undermine value to the consumer	Improve access to tariff and metering configuration information	Existing: Retail data project
4	Insufficient information about consumer profiles and consumption data	Buying groups cannot effectively bargain with retailers based on the load offerings they have	Improve third-party access to consumer profile and consumption information	Existing: Retail data project
5	Insufficient information about consumer credit history available to buying group and retailers	Retailers are wary of picking up customers who are a poor credit risk	Buying groups could 'pre-vet' consumers. Buying groups could manage credit risk on behalf of the retailers via their relationship with the customer	N/A

6	Buying groups are not providing a strong value proposition to consumers	Consumers do not engage with buying groups as they do not perceive value	Develop guidance and information to assist buying groups in understanding consumer needs and improving their value proposition	New: Fact sheets or information papers about consumer preferences and desirable characteristics of buying groups
7	Buying groups are not providing a strong value proposition to retailers	Retailers do not engage with buying groups readily or actively	Develop guidance and information to assist buying groups to understand retailer requirements and improve their value proposition	New: Fact sheets or information papers about retailer considerations and desirable characteristics of buying groups
8	Strategic and tactical hurdles	Fewer buying groups may form, and may be less successful	Highlight the opportunities represented by getting it right, in order to overcome the risks of getting it wrong. Encourage buying groups to employ small scale development approaches	New: Authority (or alternate agency) advice and guidance to buying groups
	<i>Possible regulatory barriers</i>			
9	Switching process	Limits reduce the transaction cost benefits from group switching	Review the switching process to see if changes could be made that remove limitations on group switching without compromising other areas	Existing: Review of switching process (might be out of current scope)
10	Registry structure	Complicates the group switching process	Review the registry structure and adjust it in a manner consistent with an overall market facilitation optimum	New: Registry structure re-design
11	Electricity (Low Fixed Charge Tariff Option for Domestic Consumers) Regulations 2004	Limit flexibility and innovation of group switching offerings	Review the Low Fixed Charge Regulations for overall impact on electricity market	Existing: Research project on the effects of low fixed charges

Source: Retail Advisory Group, Review of barriers to group switching and mass-market aggregation, Discussion paper, 7 April 2014, p.26.

Appendix B Potential benefits from group switching and mass market aggregation

- B.1 This appendix summarises the RAG's analysis of the potential benefits from group switching and mass market aggregation. The analysis was set out in the RAG's discussion paper.
- B.2 The discussion paper contained quantitative estimates for a subset of the potential benefits identified by the RAG. The RAG sought feedback from submitters as to whether additional work should be completed in this area, to further inform the RAG's review.

Approach to estimating potential benefits

- B.3 The RAG consulted on an approach to estimating the potential benefits from group switching and mass market aggregation, which was based on the following steps:
- (a) estimate the potential number of electricity consumers who might participate in group switching schemes. The RAG put forward a top-down approach and a bottom-up approach to doing this. The top-down approach estimated group switching numbers using overseas experience. The bottom-up approach estimated group switching numbers using the experiences of other sectors (e.g. home loan and insurance brokering) and current examples of aggregation in the electricity sector (e.g. energy services providers and the use of demand aggregation to provide ancillary services)
 - (b) estimate the cost structures of a range of aggregation models (e.g. a customer marketing channel/bundling, a dedicated buying group/broker and a charity)
 - (c) estimate the customer acquisition cost faced by retailers and assess the impact of different models of aggregator on this cost
 - (d) estimate the cost to electricity consumers from searching for better electricity deals. The RAG put forward a model for doing this, although it did not have the necessary information to populate the model. The RAG recommended that this could be an area of further work
 - (e) estimate the potential benefits of group switching stemming from a reduction in a retailer's cost to provide electricity to consumers (e.g. billing, payment collection, customer service, credit risk, electricity spot price risk).

Step 1: Estimated potential switching numbers

- B.4 Using a top-down approach, the RAG estimated that an annual switching rate of approximately 10,000 electricity consumers could be expected if mass market group switching schemes were implemented in New Zealand that were similar to those in overseas jurisdictions.¹⁷
- B.5 Using a bottom-up approach, the RAG estimated an annual switching rate of 25,000 electricity consumers. This was based on five new aggregators/buying groups being established each year, with each of these appealing to a group of 50,000 electricity consumers, and an average uptake rate of group offers of 10 percent.

¹⁷ The jurisdictions looked at by the RAG were the Australia, the Netherlands and the United Kingdom.

Step 2: Estimated cost structures of different aggregation models

- B.6 The RAG identified the following models for aggregating consumers:
- (a) customer marketing channels/bundling (e.g. ATS,¹⁸ RD1)
 - (b) dedicated buying group/broker
 - (c) an agency model
 - (d) a charity model
 - (e) an arbitrage (trader) model.
- B.7 The estimated cost to a retailer under the customer marketing channels/bundling model was \$58 - \$108 per annum per customer (for an 8,000kWh/per annum consumer).
- B.8 Under a dedicated buying group/broker model, the estimated cost to the retailer was in the region of \$320 - \$390 per customer (using a one-off payment approach), or \$268 upfront and \$73 per annum (using a trailing commission payment approach).
- B.9 An agency model does not impose a direct cost on the retailer, but instead takes a share of the consumer's private benefit. An electricity consumer nominally saving \$250 per annum by switching might pay \$45 (assuming that benefits were measured over a single year).
- B.10 A charity model is altruistic and seeks to maximise savings to the customer. It may subsidise the service so as to help its members. However, if there was no subsidisation, the estimated cost to a retailer was similar to that for customer marketing channels/bundling.
- B.11 Under the arbitrage model, the aggregator seeks to maximise profit by undercutting posted prices sufficiently to gain customers, but no more.

Step 3: Customer acquisition cost faced by retailers

- B.12 The RAG estimated the potential benefits (costs) from a reduction (increase) in the cost to retailers gaining customers to be as follows (assuming customer acquisition costs via normal marketing channels of \$150 - \$170 per customer):
- (a) customer marketing channels/bundling: a benefit of \$42 - \$112 per customer in reduced marketing costs
 - (b) dedicated buying group/broker: a cost to retailers of \$100 - \$200 per customer
 - (c) agency model: zero cost to retailer. Impact on marketing spend is uncertain
 - (d) charity model: similar benefit to customer marketing channels/bundling, from reduced marketing costs.
- B.13 The RAG concluded that overall benefits from this factor would depend on the relative penetration rates of the various aggregator models, which was very difficult to accurately model at that stage of the review.

¹⁸ Ashburton Trading Society.

Step 4: Customer search costs

- B.14 The discussion paper did not contain an estimate of the benefit from reduced search costs for electricity consumers, arising from group switching and mass market aggregation. Although the discussion paper set out a proposed model for estimating consumer savings and an increased propensity for consumers to switch, the RAG did not have to hand the information necessary to populate the model.
- B.15 This was suggested as an area for future work.

Step 5: Retailers' cost to service electricity consumers

- B.16 The RAG identified benefits from a reduction in the following costs to electricity retailers:
- (a) reduced transaction and administration costs
 - (b) reduced spot price risk from a favourable load profile for the consumer group
 - (c) a reduction in the risk of default/non-payment by customers.
- B.17 However, the discussion paper did not contain quantitative estimates of these benefits.

Appendix C Key comments and themes in formal submissions on the RAG's discussion paper

- C.1 The key comments and themes contained in formal submissions on the RAG's discussion paper can be grouped into four areas:
- (a) experience with electricity buying groups in New Zealand
 - (b) feedback on the size of the potential benefits from group switching and mass market aggregation
 - (c) potential limiting factors for group switching and mass market aggregation
 - (d) submitters' views on the RAG's conclusions and recommendations.
- C.2 Set out below are summaries of submitters' views for the first three areas listed above. Submitter's views on the RAG's conclusions and recommendations in the discussion paper are summarised in the main body of this report.
- C.3 Submitters' experience with electricity buying groups in New Zealand may be summarised as follows:¹⁹
- (a) there are a range of electricity buying groups in New Zealand, including some at a residential consumer level
 - (b) these schemes may suffer from low take-up because they do not provide individual consumers with the best deal available
 - (c) two submitters²⁰ believed the success of these buying groups depends on them presenting a sustainable value proposition, with one submitter²¹ noting this needs to offer a benefit to all three parties involved (i.e. the consumer, the retailer and the buying group organisation)
 - (d) one submitter²² believed that buying groups have struggled because of poor business models, a lack of a strong value proposition, and because they are not offering an exciting commodity
 - (e) the Electricity and Gas Complaints Commissioner noted that it had received 20 complaints about electricity buying groups.
- C.4 Submitters' views on the size of the potential benefits from group switching and mass market aggregation may be summarised as follows:
- (a) submitters were generally of the view that the benefits from buying groups are likely to be small
 - (b) three submitters²³ noted the potential for additional switching from group switching may be limited because of New Zealand's relatively high switching rate

¹⁹ This is a brief summary of the points raised in submissions. For more detail see the full summary of submissions document at <http://www.ea.govt.nz/dmsdocument/18145>.

²⁰ Genesis Energy and Meridian Energy.

²¹ Meridian Energy.

²² TrustPower.

- (c) three submitters²⁴ suggested that overseas estimates of benefits may have limited applicability to New Zealand because of differences in the markets
- (d) all of the retailer submissions noted that retailers need to consider a range of factors other than volume when making offers to electricity consumers in a buying group (e.g. credit risk, payment terms, regional/geographic location, length of contract, cost to serve). Because of this, four submitters²⁵ did not consider that volume discounts would arise for an aggregated group of small consumers
- (e) two submitters²⁶ thought it was worth considering non-price benefits
- (f) two submitters²⁷ noted the need to consider the likely duration of benefits, including how long increased switching levels could be maintained

C.5 Submitters' views on potential limiting factors for group switching and mass market aggregation may be summarised as follows:

- (a) all of the retailers submitted that there are no regulatory barriers to group switching or mass market aggregation, evidenced by the variety of current and emerging buying groups, some of which have existed for several years
- (b) four submitters²⁸ considered that any limitations represent commercial realities rather than regulatory impediments
- (c) one submitter²⁹ believed that a limiting factor on buying groups was consumers' reluctance to be bound in to a 'one size fits all' approach. Consumers are more interested in flexibility (e.g. no contract term, flexible payment terms, online self-service).

²³ Contact Energy, Genesis Energy and TrustPower.

²⁴ Contact Energy, Mighty River Power and TrustPower.

²⁵ Contact Energy, Genesis Energy, Meridian Energy and Mighty River Power.

²⁶ Contact Energy and Meridian Energy.

²⁷ Meridian Energy and Mighty River Power.

²⁸ Contact Energy, Meridian Energy, Mighty River Power and Nova Energy.

²⁹ Nova Energy.