

Testimony of Gerald A. Norlander

Executive Director  
Public Utility Law Project of New York, Inc.

On

Connecticut SB 1373

“AN ACT CONCERNING ELECTRIC RATE RELIEF”

Before the

Committee on Energy and Technology  
of the Connecticut General Assembly

March 6, 2007

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I am Gerald Norlander, Executive Director of the Public Utility Law Project (PULP).<sup>1</sup>

In 1996 the NYPSA introduced retail competition for a "supply" or "commodity" portion of natural gas and electric service, now available to consumers from either the distribution company or alternative "Energy Services Companies" or "ESCOs."

Thank you for inviting me to submit testimony regarding proposed Connecticut legislation, SB 1373. This bill contains some elements similar to measures implemented in New York by the New York State Public Service Commission (NYPSA), the purpose of which was to stimulate "migration" of customers to take "commodity" service from ESCOs.<sup>2</sup> In particular, Section 4 of SB 1373 would authorize a "retail choice and referral program" that closely resembles an "ESCO Referral Program" promoted by the NYPSA. Common features shared by the proposed SB 1373 referral program and the NYPSA ESCO Referral Program include:

- Marketing, promotion, and administrative services provided for the benefit of alternative retail suppliers at the expense of distribution utility customers;
- Incomplete price disclosure which frustrates the ability of customers to compare prices over

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<sup>1</sup> PULP is an independent nonprofit organization in Albany, New York, created by community and legal aid organizations during the 1970's energy crisis to represent the interests of low income utility consumers. Focusing on matters affecting universal service, consumer protection, and affordability, PULP frequently appears in proceedings at the New York State Public Service Commission. PULP's website is: [www.pulp.tc](http://www.pulp.tc) My biographical information is available at <http://www.pulp.tc/html/gan.html>.

<sup>2</sup> NYPSA Case 05-M-0858, *In the Matter of State-Wide Energy Services Company Referral Programs, etc., Order Adopting ESCO Referral Program Guidelines and Approving an ESCO Referral Program Subject to Modifications*, (Issued December 22, 2005).

time;

- A “teaser” short term introductory rate without disclosure of rates, terms and conditions that apply after the introductory period;
- Asymmetrical policies regarding early termination costs, with customers free to leave service provided by the distribution company at no cost, while allowing termination charges when a customer leaves an alternative provider;
- The distribution company would randomly assign to alternative providers those customers who choose to participate but do not designate a provider;
- A purchase of receivables service provided by the distribution utility to the alternative supplier which in essence converts a customer’s debt to an alternative provider into a debt to the distribution utility and could make a customer subject to termination of service due to nonpayment of amounts higher than she would have paid for full service from the distribution utility; and
- Migration “performance incentives” to provide added compensation to the distribution utility if more customers switch to commodity supply service from alternative suppliers.

I will now discuss each of these common program elements and discuss New York’s program and experience.

#### Ratepayer Subsidy of Marketing and Administrative Costs

The proposed Connecticut legislation would require ratepayers of the distribution companies to underwrite the cost of a program to promote the services of alternative providers of retail commodity service. Section 4(l) of SB 1373 provides

The department shall ensure that any and all prudently incurred costs for the implementation and operation of the programs described in subsection (k) of this section are recovered in the rates of electric distribution companies.

This is similar to what the NYPSC has done. PULP estimates that over the past ten years, more than \$100 million has been spent in New York, at ratepayer expense, to promote a retail access program that serves less than 10% of the state’s electric customers.<sup>3</sup> Over the years these efforts

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<sup>3</sup> NYPSC electric migration statistics are at [http://www.dps.state.ny.us/Electric\\_RA\\_Archives.html](http://www.dps.state.ny.us/Electric_RA_Archives.html)

have included cash subsidies to customers who switch, cash subsidies to ESCOs for each customer switched, cash incentives to the utilities for each customer who switches, cash incentives for each customer who stays with an alternative provider for one year, newspaper, radio and billboard advertising by the distribution utilities and by the NYPSC, energy fairs promoting choice of retail providers, NYPSC website promoting choice, and backout credit “adders” to reduce distribution rates for customers who switch beyond any costs avoided by the distribution utility. All of these measures have been adopted and implemented as conditions to settled distribution utility rate cases.

In addition to the NYPSC measures, interpretations of the state sales tax laws by the state tax department resulted in non taxation of unbundled delivery service for customers who purchase commodity separately, with the result that sales tax applies only to the commodity portion of a customer’s bill. This tax break may account for a larger switching percentage of industrial and large commercial customers. There has been no empirical study to ascertain whether large customers who switch providers are receiving lower cost service from alternative providers, and New York’s large industrial customers, many of whom no longer take service from distribution utilities, have expressed dissatisfaction with the rates they now pay.<sup>4</sup>

A very recent change in NYPSC policy is now reducing direct retail choice promotion

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<sup>4</sup> “What Industrial Consumers can tell the Task Force about “competition” in retail markets is that it does not exist. Industrial Consumers also believe that FERC and other federal agencies that govern energy issues are not addressing the problems that are producing rate shock for retail customers and sending signals that are so disorienting that investors and consumers alike. We further believe that the public interest has been harmed in the search for a market model that works to enable efficient competition in the electric industry.”

Comments of industrial customers (including New York’s Multiple Intervenors) to Electric Energy Market Competition Interagency Task Force on Draft Report to Congress, p. 10 (June 26, 2006). Available at <http://www.pulp.tc/ELCONComments.pdf>

and facilitation activities by the NYPSC,<sup>5</sup> but the NYPSC “ESCO Referral Program continues to place a broad obligation for retail choice promotional functions on the state’s distribution utilities. For example, in every non emergency telephone contact, New York utilities with ESCO Referral Programs are required to talk with the customer about switching providers. Obviously this adds to utility costs and takes time of customers who already have chosen not to take alternative service and are calling regarding some other aspect of service.

Similarly, the proposed Connecticut legislation would require distribution utilities to talk about alternative retail commodity providers to all new customers, and Section k(4) would require the same for customers making calls to the distribution company “for any purpose related to the customer’s electric service . . . .” SB 1373 section k(3).

Beyond possible existential benefits (and costs) of choosing for the sake of choosing, however, there is no empirical evidence that residential customers save money over time by switching utility providers or that the cost of the NYPSC promotional program is justified by any discernible benefits to consumers.

A policy issue is also presented by such programs: should significant marketing, promotion, and administrative costs for putatively competitive elements of utility service be borne by distribution company customers? In competitive industries, a dominant provider normally does not underwrite the costs of a competitor. When the dominant provider is a regulated utility, and part of the service is competitively available, ratepayers should not support

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<sup>5</sup> “The state Public Service Commission has quietly disbanded an internal group whose 15-person staff had been charged with promoting retail competition among energy and gas companies in the state. The group, known as the Office of Retail Market Development, was set up in the 1990s to ‘advocate for policies to facilitate retail access,’ letting middleman companies sell energy to homes and businesses.” *Staff to Spur Energy Rivals Gone: PSC Says Inside Unit Met its Goal, but Critic Charges Effort to Create 'Synthetic Competition' Cost Taxpayers Millions*, Newsday, Feb. 16, 2007.

advertising of any providers or class of providers, whether the incumbent or rivals.

For example, in the area of telephone service, it is not necessary for regulators to require Verizon's customers to pay for Verizon to tell its customers about the availability of service from alternative providers of telephone service, such as local, cable, wireless, or VOIP competitors. Instead, the challenge for a rival telephone company seeking to win customers away from a dominant provider like Verizon is (or should be) to provide more value. When more value is actually provided by a competitor, news quickly spreads virally to family, friends, neighbors, and in workplaces. On the other hand, when migration is induced by hype and gimmicks, when prices cannot be readily compared, when promised savings or services do not materialize, and when significant value is not actually realized by those who have switched providers, that news also spreads virally. It cannot be assumed that New York customers, who are not inclined to leave money on the table, who overwhelmingly have chosen not to take alternative utility service for a decade despite inducements and heavy advertising, are so ignorant or such creatures of habit that they would not avail themselves of new or alternative utility services that actually provide added value.

#### Incomplete price disclosure

In New York, the NYPSC only recently began to require alternative providers of natural gas and electricity to disclose their rates. This came in response to widespread consumer confusion and journalist investigations that highlighted the paucity of comparison data and the absurdity of exhorting customers to choose among providers of an essentially undifferentiated commodity without relevant price information.<sup>6</sup> The system adopted by the NYPSC, however,

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<sup>6</sup> See *Electric Choice Confounds Consumers: PSC Wants More Data on Rates Made Public*, *Binghamton Press & Sun Bulletin*, Sept. 21, 2006; *Few Switch Energy Deals: Local Utility Reports Trials Rise to 8.5%*, *Poughkeepsie Journal*, Sept. 17, 2006; *Is a Change Worth the Energy? Consumers See*

still lacks full price transparency because alternative sellers need only disclose their price once a month. Thus, they are free to change prices the next day, and so it is impossible to use the publicly disclosed data to develop meaningful price comparisons.

Similar price transparency issues are inherent in Connecticut SB 1373. Subsection two provides

Each month, participating electric suppliers shall be allowed to list introductory offers to provide electric generation service to residential and small commercial customers with each customer's utility bill. The department shall determine the manner in which introductory offers shall be made.

Under this proposed legislation, alternative sellers are “allowed” to “list” introductory offers but apparently public disclosure of all rates would not be required. As a result, price disclosure is voluntary except for the “teaser” rate in the referral program.

When price disclosure was completely voluntary in New York, many sellers simply listed the availability of their services at the PSC-funded website with a description which stated that rates are “variable.” Some of the alternative providers in Connecticut are the same providers who generally opposed any public disclosure and meaningful comparison of their prices in New York.

A “teaser” introductory rate without disclosure of post introductory period prices.

Under SB 1373, an introductory discount program would be overseen by the Connecticut DPUC, with participating sellers required to make a comparison of the introductory discount with regulated rates from the distribution company. Disclosure of rates after the introductory period – the most important information – is left for the seller to provide to the buyer later,

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*Little Benefit in Swapping Suppliers*, Binghamton Press & Sun-Bulletin Sept. 10, 2006; *Power Price Data Still Elusive: PSC Plan to Help Customers Compare Rates Draws Critics*, Albany Times Union, July 27, 2006; *Rebecca Smith, “Cranky Consumer: A Test of the Results of Electricity Deregulation,”* Wall Street Journal, March 1, 2005.

during the introductory period. At that critical time there is apparently no obligation to provide a comparison of the post introductory rate with the rate of the distribution utility. It is readily conceivable that participating customers enjoying some small savings in a program being promoted by trusted utility regulators and traditional utilities might let down their guard when they receive the boilerplate disclosure concerning post introductory rates, and not do the research needed to compare the post introductory rate with the rates of the traditional utility. Thus they may be “migrated” to new service at new rates without express agreement to the new rates, terms and conditions.

The New York “ESCO Referral Program” offers a “teaser” introductory rate to induce customers to switch. According to the NYPSC “[t]hese programs provide customers with the opportunity to obtain a 7% discount off the utility's commodity price for an introductory period when switching to an ESCO.”<sup>7</sup> If the commodity portion of a bill is, say, \$40 a month, then the New York customer saves approximately \$2.80, no matter which ESCO is selected. ESCOs in the program need not compete to provide greater savings. Only after the switch does the customer have an opportunity to learn what the rates and terms will be after the introductory period – assuming that the disclosures are timely mailed and scrutinized by the customer before the end of the period. This is a classic “bait and switch” or “cramming” tactic: baiting the customer with a temporary price break and no change in other conditions of service, and then switching to alternative, more expensive terms and conditions unless the customer affirmatively rejects them, legitimized by the NYPSC. There is no oversight of the post introductory rate

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<sup>7</sup> NYPSC “*Power to Choose*” website, <http://www.askpsc.com/askpsc/page/?PageAction=renderPageById&PageId=170e82c440a34abdc4eb7c02349bbdf8> ; *National Grid Gives Discounts to Customers Who Quit Utility*, Syracuse Post Standard, June 20, 2006.

levels or required disclosure of a comparison with regulated rates from the distribution company. The “teaser” rate followed by significantly higher post-introductory period rates, along with early termination charges, has led to significant consumer dissatisfaction in New York.

As in the NYPSC program, under SB 1373, if the customer does not react to the new terms and conditions mailed, those automatically become the new rates, terms and conditions that replace the introductory rates and they will govern the service prospectively. Because Subsection k(4) makes the mailed conditions the “default,” the burden is placed on the customer to reject the terms and conditions. In other words, it is not necessary for the seller to obtain affirmative express customer consent for the terms and conditions of service for the post introductory period. In New York, onerous provisions in the “boilerplate” of a mailed contract may provide for long durations, automatic renewals and for early termination charges if the customer seeks to return to the distribution utility or choose another competitive provider.

#### Termination Charges

Subsection (q) of Connecticut SB 1373 provides that customers are free to switch at any time to service from an alternative provider or from the distribution company. The provision is asymmetric, however, because only customers leaving the distribution utility are free to do so “without the imposition of any additional charges.” By implication, a non distribution company provider may be able to impose early termination charges or other charges if they are included in the mailed contracts that automatically take effect if the customer does nothing.

This has been a problem in New York, where customers switched providers on the basis of promised lower rates, either in the introductory rate discount program, or in telephone solicitations, only to discover that the post introductory period rates are much higher than those

of the distribution utility. Worse, when they tried to switch back to service from the distribution company, major additional charges were demanded to deter a switch back:

"The sales agent told me I could save at least \$200 a month," said Yang, who has run the Prospect Heights take-out restaurant for seven years. He also was told the "price is fixed for five years, so I could save even more in the future." So when his monthly bill shot to \$1,400, he thought there'd been a mistake. Then he learned only a portion of the bill was fixed, while an item labeled "customer charge" varied wildly. **After two months, the amount jumped from less than \$100 to an average of more than \$1,000.** Yang's ordeal has been encountered by other restaurant owners and shopkeepers who recounted similar stories to the Daily News. . . .

When Vincent Lau, owner of CA First Trading, a warehouse in Greenpoint, Brooklyn, **tried to cancel his contract with U.S. Energy, he was told the fee to do so would be more than \$10,000.**<sup>8</sup>

The boilerplate contracts, when mailed during the introductory discount period, or after a telephone solicitation, may contain many one-sided and onerous provisions that are easily overlooked by customers who trusted their state regulator and the traditional utility who may have led them to expect that competition will bring energy savings.

High rates demanded by alternative sellers are sometimes said to confer customer benefits through price stability. A careful reading of the boilerplate in the New York sellers' so-called "fixed rate" contracts shows, however, that while they lock customers in and they cannot escape the price provisions of the contract, the contracts typically give the seller one or more "outs" in case the seller finds it inconvenient to honor the contract price.<sup>9</sup>

#### Customer Assignment

In New York, the ESCO Referral program calls for the distribution company to randomly assign customers who want a discount but do not choose another provider. The proposed

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<sup>8</sup> *Electric Bills Gave Them Shock: Biz Owners Hoped to Cut Costs but New Supplier Was No Deal*, NY Daily News, Feb. 12, 2007.

<sup>9</sup> See *ESCO Contracts*, at [http://www.pulp.tc/html/esco\\_contracts.html](http://www.pulp.tc/html/esco_contracts.html)

Connecticut legislation in Subsection k(3) also provides that “[c]ustomers not expressing a preference for a specific electric supplier shall be enrolled with an electric supplier selected randomly on a rotating basis.” In New York, this provision, and the 7% standard discount reduce the need for sellers to compete on the basis of price and for market share.

Purchase of receivables and possible termination for nonpayment of excessive charges.

Subsection (o) of SB 1373 requires each distribution company to implement a “purchase of receivables” program for retail electric suppliers with full and timely cost recovery for the electric company. . . .” This is similar to what the NYPSC has required.

When the distribution utility is required to purchase receivables of commodity providers, this assures alternative providers that they can recover 100% of their charges with no bad debt. This is not an indicator of a competitive enterprise, because it shifts normal business costs of collection and bad debt to the distribution utility, and ultimately to all its ratepayers. It may also reward sharp practices that would not be undertaken if the seller had to collect all the charges demanded and deal with the customer complaints arising from enforcement of onerous provisions of boilerplate contracts.

When a receivable from a customer who fails to pay is purchased by the distribution company, then the customer owes that money to the distribution company, and is subject to the collection rights and remedies of the distribution company. Typically, a collection remedy available to utilities is termination of service for nonpayment. It is not clear from my understanding of SB 1373 whether a customer who fails to pay charges of a supplier purchased as a receivable by the distribution utility will be subject to termination of service for non payment by the distribution company, and I express no opinion on Connecticut law. In New

