

CONSUMER EDUCATION AND DISCLOSURE POLICIES

What if state and federal policymakers restructure the electric industry to create a competitive market, but participation by residential and small commercial customers is much lower than expected? A competitive market needs both willing buyers and sellers. If buyers don't participate in the competitive market, the ability of the competitive market to exert a better discipline on prices than traditional utility price regulation will be impaired. Indeed, if customers do not shop for electricity or suppliers do not market to residential customers, there is a real risk that the promise of competitive markets for electricity will not be realized. In a worst case scenario, the result may be the unintended creation of an unregulated monopoly or oligopoly.

While many key decisions that will impact the creation of a competitive market are not the subject of this *Blueprint*, two initiatives may go far to help stimulate customer interest in competition and help consumers develop the skills to shop for electricity. The first initiative focuses on how consumers learn about the move to electric competition. The second initiative focuses on giving consumers the tools to enter the competitive market and make an informed choice. The judicious use of disclosure requirements that enable customers to

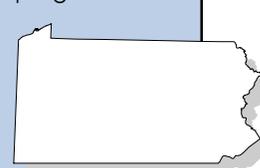
shop and compare offers, can help prevent fraud and abuse, and provide a form of regulatory investment that may prove cheaper than enforcement proceedings in a hearing or court room.

Consumer Education

Most residential and small business consumers routinely pay their monthly electric bill without much attention to regulated rates or usage patterns. Indeed, recent research reveals that most consumers do not know their annual energy usage or the price paid per kWh on their utility bill.¹ Residential households use far less energy than commercial or industrial customers and the annual residential energy bill (65% of which is electricity for households) typically

A customer who asked to be part of the **Pennsylvania** electric pilot programs in November, 1997, had this reaction to the offers that appeared in his mailbox from electricity suppliers, "Each had different information, a different pitch--you couldn't compare apples to apples." The customer felt that participating in the pilot program took more time than it was worth in potential savings.

"The Outlook," Timothy Appell, *Wall Street Journal*, December 15, 1997.



consumes 5% or less of household income.² Even in states with higher than average electricity rates, such as the New England states where residential rates average 11-13 cents per kWh, the monthly electric bill is still a relatively small portion of a typical residential customer's monthly budget. While residential customers often are concerned about electricity prices, the move to retail electric competition is not being driven by their concerns. Because of this, some observers believe that residential customers will not participate extensively in the new competitive market, especially when their initial savings may be 10% or less compared to current annual costs. Will customers be naturally inclined to shop and compare prices when savings on their bills during the early years may not exceed \$5 to \$10 per month? Will low-income, elderly and non-English speaking customers obtain the information necessary to understand an issue that appears complex, with a daunting new vocabulary, and that at first glance appears to threaten the reliability of their electric service?



Even though the long distance telephone market was first opened to competition in 1984, AT&T still had over a 50% market share in 1996.

Telephone Restructuring: A Case Study

Policymakers are looking to lessons learned from restructuring of the telephone industry, which began with the break-up of AT&T and the onset of long distance telephone competition in 1984. In telephone industry restructuring, neither federal or state regulators undertook any significant public education campaign to prepare customers for changes. Once long distance telephone competition began, it produced a litany of complaints by residential and small business customers, alleging that their long distance service providers had been changed without their permission, a practice known as "slamming." Telephone customers also complained about aggressive marketing tactics, such as telemarketing calls during the dinner hour, or the high prices of some credit card and operator-assisted calls at pay phones. Many telephone customers also questioned the prices charged by some companies for pay-per-call services (1-900 calls) that appeared on their local phone bills and threatened the continuation of local phone service if the unregulated charges were not paid.

These developments have, in turn, resulted in legislative and regulatory efforts to belatedly address consumer protection and education issues associated with telephone restructuring. Customers have reacted to questions about electric restructuring by raising these same concerns and asking for protections to prevent their reoccurrence.

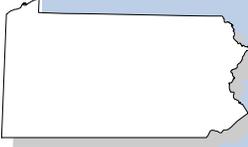
The Implications for Electric Restructuring

Many states have concluded that the move to electric competition will require a larger educational effort than the traditional utility bill inserts or public hearings and workshops. Preparing customers to shop for electricity and then respond to marketing messages they receive will require a comprehensive and professional outreach and educational effort. Customers will need frequent messages from a variety of sources to understand their new rights, responsibilities, and opportunities. Outreach and education will probably require additional resources, since most state regulatory commissions have not had to conduct such efforts in the past. The dramatic change in relationship between customers and their electric utility cannot be accomplished by relying solely on the tools that have prevailed in a monopoly utility structure.

The purpose of a comprehensive public education program should be to maximize public participation in the implementation of retail competition, minimize customer confusion about the changes being undertaken, and equip *all* customers with the means to participate effectively in the competitive electric market. While any state-funded educational effort must be neutral and objective, it should not be confused with the promotional and brand name marketing efforts of competitive suppliers. Customer education and outreach programs in several states have been designed to motivate customers to learn about electric com-

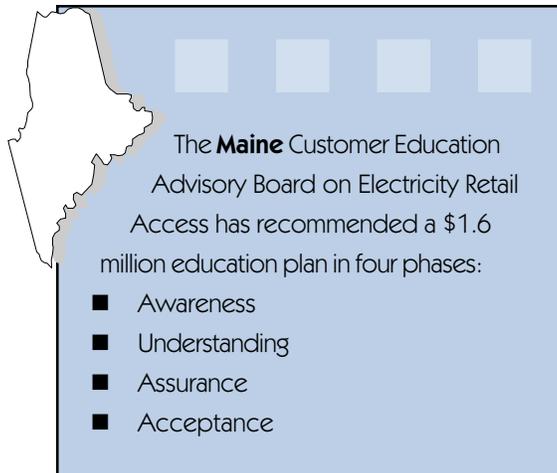


California's PUC has initiated a \$90 million state-wide education program called "Plug In, California!" to stimulate customer awareness of competition. This program, funded by distribution utilities through rates charged to all customers, is designed to inform customers with TV and radio advertisements, followed by a direct mail campaign targeted to every household. In addition, more than \$13 million is available to community-based organizations to focus on local education activities, especially for low-income, rural, and elderly customers.



The **Pennsylvania** PUC has ordered all distribution utilities to fund comprehensive consumer education programs with a statewide multi-media campaign and a local education effort that involves community organizations. The PUC has set program funding levels for each utility at \$5 per customer over a 4-year period.

Careful attention to timing, educational messages, information disclosure, and assurance of consumer protections will accelerate the development of competitive retail markets for electricity and help ensure that the benefits of lower prices, more choices, and better service are available to all consumers.



petition with modern marketing techniques. Key components of a well designed electric competition education program have included:

- information dissemination by means of interactive activities, as well as brochures or other written materials, and use of a variety of mass media outlets, with the intent to motivate the public to become interested in, and learn more about, electric competition;
- explanations in clear language (and multiple languages in some states) of the basic concepts of electric restructuring, which include (1) information on how prices, consumer protections and low-income programs may be affected; (2) explanations of customer risks and responsibilities; (3) information about how to assess and make use of a household energy profile to shop for electricity; (4) how to compare offers from electric suppliers; (5) information about aggregation; and (6) information about dispute resolution mechanisms, including the role of state agencies
- in resolving disputes with retail electric suppliers;
- well-publicized public forums conducted in several geographical areas to obtain public input and provide opportunities for information exchange;
- active involvement of community organizations in developing messages and devising and implementing education strategies, particularly for low-income, elderly, foreign speaking, rural and other customers who may miss more traditional media-based efforts;
- use of focus groups and surveys to gather public input on both broad restructuring issues and concerns, as well as on public education needs and reaction to initial outreach initiatives;
- a toll-free hotline to provide guidance to consumers seeking advice about personal energy needs, the selection of a retail supplier, aggregation, or dispute resolution; and
- use of pre-established outcome measures of customer awareness, understanding and ability to act, which periodically evaluate education and outreach efforts.³

In states that have designed comprehensive electric restructuring education programs, the state public utility commission has taken a leadership role in coordinating, funding,

and implementing the program, although usually with a broad-based advisory committee or other public involvement process. While there are several funding options, such as state tax appropriation, increased commission budget, or funding via the distribution utility's rates, most states have opted to fund their education program through imposition of transition costs on distribution utilities.

Shopping for Electricity

The arrival of customer choice carries with it the potential for customer confusion. If the experience in other industries is any guide, comparing electricity pricing offers will be especially confusing and difficult. Is \$5 a month and 10¢ per kWh better than \$10 a month and 8¢ per kWh? Or \$6 and 12¢ per kWh with a 40% off-peak discount? Furthermore, the sale of electricity itself may be bundled with other products, such as alternative meters (which will offer additional energy management services or pricing options), or even other products, such as Internet access or telephone services. Product linkages may make comparisons among offers by multiple suppliers even more difficult.

In some industries, such as consumer credit, appliances, cars, and food,⁴ uniform consumer disclosures have been developing for decades.⁵ This author has suggested that the lack of uniform price disclosure on bills and other marketing materials in the long distance telephone industry may have contributed in part to the lack of significant gain in market share

for AT&T competitors for over a decade.⁶ This same development may occur with the move to electric competition unless there is a concerted effort to adopt a different approach. The primary problem is that consumers lack both critical information and skills to easily evaluate different price offers. Furthermore, consumers have a long-standing habit of receiving their electric bills and paying them automatically. Nothing more has been expected of customers in a regulated market. If consumers do not take the time to shop in a competitive market, they cannot fulfill their essential role in making competition work in favor of the most efficient suppliers (or those suppliers promoting attributes other than price which may be valued by some consumers, such as environmentally friendly products or energy sources located in the consumer's state). In the absence of key consumer information, the marketplace works on the basis of information manipulation rather than

Maine's Consumer Education Program

Rule requires distribution utilities to fund a Commission-approved \$1.6 million consumer education program for electric restructuring over a four-year period. The assessment will be recovered from ratepayers. "This funding determination is based on the principle that those consumers who benefit from a program should pay to support it."

Order Adopting Rule, Docket No. 97-

efficiency. This is particularly true for consumers whose monthly bill for electricity or telephone is a modest part of the household budget.

Recognizing this, the National Association of Regulatory Utility Commissioners (NARUC) in July 1996 urged states adopting retail direct access programs to include enforceable standards of disclosure and labeling that would allow retail consumers to easily compare the price, price variability, resource mix, and environmental characteristics of their electricity purchases.

Among other purposes, NARUC announced its belief that

“the electric industry should facilitate informed customer choice that will promote efficient markets.”

What Should Be Disclosed

Consumer research has confirmed that the public wants comparative price information. Focus groups and surveys in New Hampshire and Massachusetts of customers who had participated in pilot electric competition programs, documented confusion with the lack of standardized pricing statements and called for state regulation to provide standard price disclosures.⁷ As a result of this experience, utility commissions in New England have worked together to develop a model, uniform Electricity Disclosure Label and a more detailed *Terms of Service* document for the sale of electricity to residential and small commercial customers to be used by

suppliers marketing in the New England region. The following discussion summarizes key recommendations of this collaborative effort.⁸

Price

Customers should be able to compare prices on an “apples-to-apples” basis. The most commonly recommended approach is to disclose the supplier’s price structure in a cents per kWh for 3-4 common usage levels (i.e., 500, 1000 and 2000 kWh levels for residential customers). One key policy issue is whether a uniform price disclosure method should reflect only the competitive generation service offered by the supplier or include all other pieces of the customer’s monthly electric bill, i.e., distribution charges and possibly other unregulated services. Limiting price disclosure to generation services allows suppliers selling across a wide geographical area to use a single label without regard to differences in distribution charges. If distribution costs are included, it is impossible to include a label, for example, in a *Boston Globe* ad that reaches consumers in other utility service areas.

If suppliers are required to provide average price information at several typical usage levels, most customers can identify a level most closely matching their own. One-time cash rebates or other price inducements should probably not be reflected in the disclosure of average electricity price. Prices for time-of-use (TOU) rates should be based on consistent load profiles for customers, with usage levels shown. If a supplier uses variable prices in which prices

change according to an index, the disclosure could show prices reflecting a recent period or project under a uniform set of assumptions, much like variable rate consumer credit contracts (including mortgages) under the Truth in Lending Act rules.⁹

Contract Terms

In addition to price, consumers will need to know the contract duration and whether the price is fixed or variable over the term of the contract. Other important terms include penalties for early termination, late fees, or other extra charges. Because consumers are unlikely to actually sign a contract document to buy electricity, it will be important for consumers to know and understand the *material* terms of their agreement. After all, consumers will no longer be able to rely on the tariffs filed by their current utility with the public utility commission (a form of “master contract”) for their purchase of electricity in a competitive market.

Supply Mix

Consumers are concerned about the environment, and want information about fuels used to generate electricity.¹⁰ One supplier’s electrons will not automatically flow only to the homes of its own customers. Rather, the local power pool will probably dispatch sufficient electricity to meet local demand based on cost and reliability factors of the total generation mix. Nonetheless, if more customers buy from “green” suppliers, renewable power will be an increasing part of the local power mix. Therefore, several states are working to develop a method

of disclosing fuel mix on electricity product labels, showing major fuel types (coal, oil, nuclear, renewable energy) as a percent of the supplier’s total generation mix. For example, California requires all suppliers to disclose their fuel mix based on an historical record.¹¹ If a supplier obtains “generic” power from the regional power pool, the fuel mix disclosure should reflect that power mix or a comparable substitute. If the supplier proposes to market power from a particular facility, the fuel source for that facility could be presented.

Emissions

Massachusetts has recently adopted regulations that require suppliers who market in that state to disclose price, fuel mix, and air emissions (sulfur dioxide, nitrogen oxides and carbon dioxide).¹² A supplier’s generation source emissions must be expressed in a form which compares them to average regional emissions of all generating sources. This approach allows customers to compare a supplier’s emissions profile with other power generators.

Labor

Massachusetts’ electric restructuring law also requires suppliers to disclose the percentage of their generation mix that comes from power sources with employee union contracts and the percentage that comes from power sources that use replacement labor during labor disputes.

When Disclosures Should Be Provided

Terms of Service Document.

In addition to price, contract length, supply mix, and emissions data, other key disclosures that states should consider requiring suppliers to highlight in a *Terms of Service* document include:

- All additional fees, including early termination penalties or late fees
- Deposit policy
- Collection procedures, including right to payment arrangements, and special programs available for low-income customers, if any
- Supplier's dispute or complaint handling policy, including the state commission's toll free complaint number
- Limitations and disclaimers of warranties
- If applicable, the customer's right of rescission and how to exercise this right

There are at least three distinct events or points of contact in a customer's relationship with an electricity supplier that suggests a need for different disclosures. Suppliers should disclose information to their customers (or potential customers) in (1) promotional materials; (2) *Terms of Service* documents or contract summaries; and (3) monthly bills.

The first point of contact is at the time a supplier advertises its electricity products. Drawing comparisons to a requirement of the Truth in Lending Act, some experts recommend development of an Electricity Facts Label with disclosures concerning price, fuel mix and emissions (or other required items), which should appear in a supplier's printed advertisements and written promotional materials.¹³

A second point of contact is at the point when a customer enters into a contractual relationship with the supplier. In contractual terms, the supplier has made an offer which the customer has accepted. After the agreement is made, the supplier must inform the customer about the material terms of the agreement in order to have a legally enforceable contract. This can be done in a *Terms of Service* document, which should contain all the material terms of the contract, including the supplier's pricing method, fees, and complaint procedure. In California, Pennsylvania and Maine, the *Terms of Service* disclosure must also offer customers a "right of rescission" to cancel the contract without penalty within 3-5 days. If this right is prominently disclosed in the *Terms of Service* document, customers may examine the price and other contract terms in detail before deciding to continue the contractual relationship.

The third point of contact during which information should be disclosed is in the supplier's bills. Customers will receive a bill either directly from the supplier (which may or may not include the distribution/transmission portion of the bill) or as part of the customers' distribution company bill. At this point, customers would want to know the actual cost per kWh for electricity used during that billing period. Doing so would require suppliers to divide their customers' charges for electricity by total kWh usage. Note that such a disclosure requirement is not a substantive regulation of a supplier's rate design or pricing method. This proposal would allow customers to see the effect of their suppliers' price design on their own usage patterns.