

STATE OF NEW YORK  
PUBLIC SERVICE COMMISSION

At a session of the Public Service  
Commission held in the City of  
Albany on January 23, 2002

COMMISSIONERS PRESENT:

Maureen O. Helmer, Chairman  
Thomas J. Dunleavy  
James D. Bennett  
Leonard A. Weiss  
Neal N. Galvin

CASE 00-M-0504 - Proceeding on Motion of the Commission  
Regarding Provider of Last Resort  
Responsibilities, the Role of Utilities in  
Competitive Energy Markets, and Fostering  
the Development of Retail Competitive  
Opportunities - Unbundling Track.

ORDER CONCERNING ESCO DEPOSITS AND PREPAYMENTS

(Issued and Effective May 9, 2002)

BY THE COMMISSION:

INTRODUCTION

This Order requires Energy Service Companies (ESCOs) to provide evidence of creditworthiness before requesting deposits or prepayments from their customers. Satisfactory evidence is a sufficient bond rating from an independent rating agency (for either the ESCO or its parent, if the parent agrees to act as guarantor for the ESCO). Additionally, ESCOs not able to provide a bond rating may request deposits if they have a letter of credit or escrow account with a financial institution with at least an A credit rating.

PROCEDURAL HISTORY

On May 9, 2001, we issued for comment a staff proposal to require ESCOs to establish creditworthiness before requesting

prepayments or customer deposits.<sup>1</sup> Comments on the staff proposal were received from Community Power Network of New York State, Inc. (CPN), an energy consumer advocate; Con Edison Solutions (CES); NYS Consumer Protection Board (CPB); Local 1-2, et al. (Unions); National Fuel Gas Distribution Corp. (NFG); New York Energy Service Providers Association (NESPA); New York State Electric & Gas Corporation (NYSEG); North American Energy, Inc. (NAE); Office of the Attorney General (DOL); and Public Utility Law Project of New York, Inc. (PULP). The parties commenting on the staff proposal raised several concerns. In this order, we require that ESCOs provide evidence of creditworthiness before requesting prepayments or deposits.

#### COMMENTS AND DISCUSSION

##### Applicability of HEFPA

CPB, NYSEG, DOL, and PULP would require ESCO consumer protections that are consistent with those imposed on the utilities under the Home Energy Fair Practices Act (Public Service Law Article 2) (HEFPA) and the Commission's non-residential rules. The issue is under consideration in the Competitive Markets proceeding;<sup>2</sup> and we will address it there.

##### Documentation of Financial Viability

Several parties were concerned that the use of an ESCO's documentation of financial viability to provide security for return of deposits and prepayments to customers might not sufficiently protect customers in case of ESCO bankruptcy or departure from the market. These parties stated that ESCO

---

<sup>1</sup> Case 00-E-0504, Competitive Opportunities, Notice Soliciting Comments (issued May 9, 2001)

<sup>2</sup> Case 00-M-0504, supra.

financial viability may fluctuate and that a one-time demonstration of financial viability may not remain a viable protection over time.

CPB and PULP recommended that the Commission forbid ESCOs from using any demonstration of financial viability to satisfy the evidence requirements. NYSEG stated that the use of statements of financial viability would be unlikely to provide significant protection for customers. The Unions recommended that the Commission require that updates to reports of ESCO financial viability be made at least once every two years, preferably annually.

The Uniform Business Practices allows ESCOs to satisfy credit requirements for utility delivery charges by establishing a minimum bond rating standard, or, as an alternative, Dun and Bradstreet (D&B) ratings in conjunction with payment history.<sup>3</sup> Because some ESCOs may not have payment histories, the D&B rating and payment history combination is not feasible for them. The proposed bond rating standard would provide the best available evidence of financial viability. Accordingly, we direct utilities to file revisions to their retail access tariffs and operating agreements that require utilities to allow an ESCO to accept prepayments from its customers only if it submits the required bond rating evidence required by the Uniform Business Practices.<sup>4</sup> The revisions would also require utilities to allow an ESCO to accept deposits from customers if it submits the required bond rating, or escrow account or letter

---

<sup>3</sup> Case 98-M-1343, Retail Access Business Rules, Order Granting Portions of Petition for Rehearing (issued April 15, 1999), Appendix A, p.3, first item in § B(1).

<sup>4</sup> That is, a minimum rating of "BBB" from S&P, "Baa 2" from Moody's or "BBB" from Fitch. Case 98-M-1343, supra, Appendix A, p.3, § B(1).

of credit evidence. Finally, the suggestions for requiring annual submissions of bond ratings are well taken. ESCOs seeking to collect prepayments or deposits from their customers, shall submit required evidence to utilities on August 1, 2002 and on August 1 of each subsequent year.

Maximum Deposit Level

The staff proposal provided that an ESCO generally may not require a residential customer to deposit as security an amount of money greater than twice the average monthly bill for a calendar year. The proposal also required ESCOs to submit evidence that the money would be used for customer benefit.<sup>5</sup> The staff proposal would have applied to ESCOs essentially the same limitation on deposit amounts that HEFPA and the non-residential rules apply to utilities.

The ESCO parties (CES, NESPA, and NAE) argue that the two-month limitation is insufficient to provide them financial protection and propose various remedies. CES and NESPA note that, if deposits are appropriately secured, no additional customer protection is provided by limiting the size of the deposit. They recommend allowing ESCOs and customers to agree on the appropriate level of security deposit in contractual agreements. NAE proposes to increase the deposit limitation to triple the highest customer bill and change the Uniform Business Practices to shorten the amount of time it takes to return a customer to the utility. In support of the deposit requirement, PULP notes that customers "perceived as credit risks, by failing to pay lawful bills" may benefit from "an alternative method of

---

<sup>5</sup> Case 00-E-0504, supra, Notice Soliciting Comments (issued May 9, 2001), Appendix, unnumbered page 1.

qualifying for service from the ESCO," that is, a deposit to secure service.

NYSEG raises an additional deposit issue. It believes that ESCOs have sought information regarding utility-held customer deposits with the intention of requesting a transfer of the deposit amount related to commodity from the utility directly to the ESCO. NYSEG recommends that such deposit transfers be prohibited.

ESCOs should be allowed to request deposits of their customers. Unless ESCOs are allowed to protect themselves from the risk of non-payment, poor credit customers may not get many offers from competitive providers. We agree with CES and NESPA that, as long as deposits are appropriately secured and customers can continue to obtain service from the utilities under HEFPA guidelines, allowing ESCOs and their customers to negotiate appropriate deposits is reasonable. We will revisit this issue if abuses become apparent. NYSEG's opposition to deposit transfers is reasonable. It is important that customers not confuse deposits for regulated utility service with deposits for other services. Deposit arrangements are an important aspect of utility service because the deposit funds are customer monies. Thus, we will prohibit deposit transfers.

#### Sufficiency of Financial Instruments

In addition to demonstrations of financial viability, the staff proposal would have allowed an ESCO to satisfy the evidence standard for deposits by establishing a variety of financial instruments, including letters of credit, escrow accounts, bonds, and certificates of deposit. NAE indicated that an ordinary escrow account should be sufficient evidence. NFG and PULP believe that additional language is required to ensure that the financial instruments strictly segregate customer monies from the ESCOs' assets and ensure that such

funds are not available for commingling in the case of ESCO bankruptcy. CPB would restrict use of the funds. It would allow an ESCO to use these customer funds for any purpose other than to refund a deposit, only if it provided a five-day notice to staff. It describes the notice requirement as an "early warning signal" of ESCO financial difficulties for the Commission.

We will allow the use of only an escrow account or letter of credit from an "A" rated financial institution to secure customer deposits. An escrow account or letter of credit provides greater assurance that the funds would be available than other types of financial instruments. We will allow the use of escrow accounts and letters of credit, less secure credit assurances than a minimum bond rating, for deposits because the amount of deposits is more limited. Prepayments, on the other hand, may consist of a larger customer payment to an ESCO, perhaps payment of service for the entire year, and, thus, present a risk of greater loss. Therefore, we will permit ESCOs to accept prepayments only upon presentation of documentation of a minimum bond rating described above.

#### Ban on Prepayments

One party, CPN, recommends that the Commission forbid ESCO prepayments/deposits entirely. We believe, however, that a ban on all prepayments might stifle market innovation and deprive customers of some of the potential benefits of competition. Adherence to the creditworthiness criteria discussed above furnishes adequate protection for customers.

#### Interest on Deposits

CPB favors requiring ESCOs to pay interest on customer deposits equal to the ESCOs' borrowing rate. ESCOs may choose to differentiate themselves by offering different rates of

interest on amounts held for deposit. We will allow more time for market responses to develop before considering whether it is necessary to fix an interest rate for ESCO deposits.

#### Reporting Requirements

In its proposal, staff does not specify what reporting would be required or preferred for ESCO records of customer deposits and prepayments. It would, however, require ESCOs to maintain this information and be prepared to make it available for inspection, "and to file a report thereon in the manner, and form the Commission may require." CES is concerned that the proposed requirement would impose an unnecessary administrative burden and states that it is sufficient for an ESCO to provide this information upon request within a specified time period. The staff proposal is consistent with the CES recommendation in that it proposes that we require no specific manner of or time for reporting the information. The report would be filed, upon direction of the Commission.

#### Notification Requirements

CPN proposes that we require ESCOs to provide notice to their customers describing the methods used to secure customer deposits and prepayments and stating that the ESCO will return them in the event that ESCO discontinues service for any reason. We agree. ESCOs are directed to provide the notice to a new customer before the customer makes a deposit or prepayment. The ESCO shall notify existing customers by providing copies of revised disclosure statements and/or contracts that contain the information in the notice. ESCOs are required to file an example of the revised disclosure statement and/or contract with staff prior to distribution to customers. The information in the notice and revised disclosure statements and/or contracts would include: a description of the credit

evidence or escrow account, or letter of credit submitted by the ESCO; applicable interest rate, if any; conditions for use of customer funds; circumstances that allow use of the funds for payment of customer bills; and, conditions for return of funds.

Applicability to Non-Residential Customers

CPB believes that small commercial customers do not have the same level of sophistication as large commercial and industrial customers to negotiate contracts that will adequately protect them from the concerns this proposal was developed to address. CPB recommends that the proposed consumer protections be extended to small commercial customers as well as residential customers, since the best available evidence indicates that these customers are similarly vulnerable to the kinds of abuses that can and have occurred. NYSEG agrees, but it would extend these protections to all non-residential customers.

CPB's position that residential and small commercial customers may be at similar risk of loss of security for advanced payments and deposits is reasonable. Small commercial customers are similar to residential customers in that their lack of resources may prevent negotiation of contract terms that would protect them from loss of prepaid funds. For these reasons, we will extend the proposal to cover small commercial customers.

Extending the protection to non-residential customers, as recommended by NYSEG, could create additional burdens for ESCOs. Further, the greater sophistication of larger customers should require less regulatory oversight to prevent abuses. The proposal will therefore be modified to include small non-residential customers. Because utilities may not have a distinct small non-residential service classification, there may be a need to develop a special standard for this purpose. ESCOs, seeking to offer prepayment agreements or require

deposits from their customers, should review utility customer class descriptions to distinguish small business customers from larger commercial and industrial customers for the purpose of applying this provision.

#### Applicability to Budget Billing

NFG would explicitly include budget-billing plans in the staff proposal, as well as prepayments and deposits. Extending the security requirement to budget billing plans is unnecessary and unduly burdensome. Prepayment plans typically require customers to post payment for several months' worth of service in advance, while customers on ESCOs' budget billing plans would have relatively smaller credit balances and, at times, may owe the ESCO money, rather than the reverse. In addition, there is no evidence that a significant number of ESCOs have offered budget or levelized payment plans, nor that they have an adverse effect on customers. Therefore, there is no need to extend the financial security requirements to budget billing at this time.

#### Third Party Liability

NYSEG seeks assurances that utilities and customers would be held harmless in the event of ESCO default on prepaid or deposited amounts. NYSEG is particularly concerned that utility-held assets of the defaulting ESCO that rightly belong to either itself or other customers not be used to ameliorate damage caused to customers by loss of prepayments.

The legal rights to funds held by a utility or its customers are not changed by an ESCO's failure to refund prepayments and deposits. This Order establishes credit requirements for permitting an ESCO to accept prepayments and deposits. Its purpose is to establish conditions that

discourage or prevent an ESCO's failure to provide refunds to its customers.

The Commission orders:

1. Each gas and electric utility (KeySpan, Central Hudson Gas & Electric Corporation, Consolidated Edison Company of New York, Inc., Corning Natural Gas Corporation, National Fuel Gas Distribution Corporation, New York State Electric & Gas Corporation, Niagara Mohawk Power Corporation, Orange and Rockland Utilities, Inc., Rochester Gas and Electric Corporation and St. Lawrence Gas Company, Inc.) shall file tariff revisions designed in accordance with the foregoing Order, to become effective on a temporary basis on not less than one day's notice within 30 days of the issue date of this Order.

2. The requirement of Section 66(12)(b) of the Public Service Law as to newspaper publication of the tariff revisions is waived.

3. This proceeding is continued.

By the Commission,

(SIGNED)

JANET HAND DEIXLER  
Secretary