

EXECUTIVE SUMMARY

Electric and natural gas utilities in numerous states have sought to replace traditional “credit-based service” with “prepaid service” delivered through prepayment meters or advanced, digital meters with remote disconnection and reconnection capabilities. (See map of the United States on page 6 identifying currently-operating prepaid service programs.) Traditionally in the U.S., electric and natural gas service has been billed on a post-paid basis where a utility company tracks a customer’s usage during the previous monthly or quarterly period and then mails a bill to the customer based on that usage. The customer is then required to make payment within a predetermined time frame or face disconnection procedures. In most states a utility must offer a customer facing disconnection a payment plan to pay down an arrearage over a period of months while retaining access to service.

Prepaid service, as the name implies, requires customers to pay in advance for their service with prepaid account balances decreasing as service is delivered. In most instances, service is automatically suspended when account balances are depleted. While consumers using prepaid service may receive electronic notification that billing credits are running low, there is no obligation on the part of the utility to deliver shutoff notification securely through the mail, to continue providing service for some period of time (e.g., days or weeks) after credits are exhausted, or to work with payment-challenged customers by offering reasonable payment plans or other means of retaining access to basic utility service.

The movement to prepayment allows companies to sidestep critical consumer protections that have evolved over decades while altering the utility’s incentives to interact creatively and constructively with payment-troubled customers. State legislators and utility regulators have long recognized that utility service is a necessity of modern life and that loss of service poses a threat to health and safety. Toward this end, they have adopted important utility consumer protections regarding bill payment timeframes, and secure, reliable notification by mail prior to disconnection of service. Many states help to ensure utility bill affordability through discounted rate structures and “arrearage management” programs. In some states, consumer protections include prohibitions or limitations on residential customer late payment fees and security deposits. The movement to prepayment effectively guts these important consumer protections.

Experience in the United Kingdom and the United States demonstrates that prepaid metering and billing is targeted toward and concentrated among low- or moderate-income consumers, particularly those who are facing unaffordable security deposit requirements or disconnection for nonpayment under traditional service. In the largest prepayment program operating in the United States (Arizona's Salt River Project's M-Power program), prepaid electric service is increasingly concentrated among racial minorities. Additionally, prepayment results in more frequent service disconnections or interruptions (a 1997 customer service survey conducted by Centre for Sustainable Energy National Right to Fuel Campaign found that 28 percent of prepayment

customers in Great Britain were disconnected from service over the past year). Also, customers sometimes pay higher rates than they would under traditional credit-based service. Low-income customers using prepaid utility service tend to make numerous, small payments on a monthly basis to retain electricity or natural gas service, often incurring transaction fees that add to the customer's total cost for basic service.

Households with the least means are trapped under prepayment, often paying higher costs and transaction fees while experiencing more frequent, disruptive, and dangerous loss of service. Such a system creates a two-tiered system, favoring wealthier, credit-paying households.

Increased disconnections of gas and electric service that come with prepayment threaten the health and safety of customers, particularly the elderly, disabled, and low-income families with children. Disconnecting natural gas or electric service has caused house fires and extreme indoor temperatures, which can result in illness and death. Implementing prepaid utility service, with the increased rates of service disconnection that result, increases the risk that such tragedies will occur.

With prepaid utility service, low-income customers who struggle to pay their bills often end up paying more for second-class utility service. Access to essential service, delivered by regulated, franchised monopoly utility companies, should not be compromised by a service model that leads to the forfeiture of regulatory consumer protections. **Rather, payment issues related to the inability of some households to afford a basic level of uninterrupted utility service should be addressed through delivery of comprehensive, effective low-income energy efficiency programs, bill payment assistance and “arrearage management” programs, reductions of burdensome late payment fees and security deposits, and implementation of deferred payment agreements that are truly reasonable and based on a household’s actual income and expense circumstances.**

The advent of advanced metering infrastructure (AMI) and digital meters, commonly called “smart meters,” dramatically increases the potential for new utility prepayment programs. Advanced meters—which include remote disconnection and real-time communication capabilities—obviate the need for utility companies to invest in “standalone” prepayment meters, and reduce the related upfront capital investment required to implement a new prepayment program. The recommendations that follow are based in large measure on provisions of a resolution adopted by the National Association of State Utility Consumer Advocates on June 11, 2011.

Recommendations

The National Consumer Law Center opposes prepaid electric and gas services. However, if a company is allowed to implement prepaid service, state regulatory commissions should require each of the following provisions.

1. **Regulatory consumer protections and programs should be maintained or enhanced.** These include existing limitations or prohibitions on disconnection of service, advance notice of disconnection, availability of payment plans, availability of bill payment assistance or arrearage forgiveness, and the right to dispute bills.
2. **Health and safety risks must be reduced.** When the billing credits of a customer receiving prepaid residential electric or natural gas service are exhausted, the customer must be given a five-day disconnection grace period, after which the customer must be restored to traditional, credit-based service, subject to all rules and customer protections applicable to such service. Prepayment customers should be allowed to return to credit-based service at no higher cost than the cost at which new customers can obtain service.
3. **Vulnerable populations must be protected.** Prepayment service should not be offered to low-income households or households that include any person who is elderly, disabled, or who has a serious illness. Households with young children should also not be eligible to enroll in prepayment service.
4. **Marketing of service should be voluntary.** Prepaid service should only be marketed as a voluntary service and should not be marketed to customers facing disconnection for non-payment. Conditioning service on the method of payment is not marketing—it's coercion.
5. **Payment assistance and arrearage management programs must be adopted or maintained.** Utilities offering prepaid service to low-income customers must also offer effective bill payment assistance and arrearage management programs to those customers.
6. **Rates for prepaid service should be lower than rates for comparable credit-based service.** This lower rate reflects the lower costs associated with reduced carrying costs, collection costs, uncollectible accounts, and shareholder risk.
7. **Costs should be transparent.** Prior to implementation, utilities should demonstrate the cost effectiveness of any proposed prepaid service program and reveal how costs will be allocated among various classes of customers.
8. **Transaction and other junk fees should be eliminated.** Prepayment customers should not pay security deposits or additional fees that traditional customers are not required to pay. Examples of such fees include initiation fees, equipment charges, or transaction fees to purchase billing credits, or frequent payment fees.
9. **Initiate “on demand” service.** Utilities must ensure there are readily available means for prepayment customers to purchase service credits on a 24-hour a day, seven-day a week basis to prevent potential health and safety risks.

10. **Tracking and reporting should be monitored and disclosed.** Prepaid service programs should be monitored to ensure there is not an increased rate of service disconnections for non-payment. Utilities implementing prepaid service programs should track and report to the state regulatory commission on a monthly basis the following data *separately for credit-based and prepayment residential customers*:
 - Number of customers
 - Number of customers with arrears of 30 days or more
 - Dollar value of arrears
 - Number of disconnection notices sent
 - Number of service disconnections for non-payment
 - Number of service reconnections after disconnection for non-payment
 - Number of new payment agreements entered
 - Number of payment agreements successfully completed
 - Number of failed payment agreements
11. **States should proactively plan for customer protections in case of company default.** States must have adequate financial mechanisms to guarantee that funds prepaid by customers are returned to customers if a company becomes insolvent, goes out of business or is otherwise unable to provide the services for which the funds were prepaid.

Conclusion

In service territories where prepaid service is already implemented, the implementing utility should answer a series of customer service questions on an annual basis. A list of those questions may be found in Appendix A (page 27).

With prepaid utility service as it currently operates, low-income customers who struggle the most to pay bills often end up paying the most while receiving second-class utility service. Access to essential life-supporting service, delivered by regulated, franchised monopoly utility companies, *should not* be compromised by a service model that allows companies to sidestep important consumer protections that were implemented for health and safety reasons. Instead, payment issues should be addressed through delivery of comprehensive, effective programs and policies that account for a household's actual income and expenses, rather than a punitive prepaid program.

If a utility company is allowed to roll out a prepayment program, it is critical that state governing bodies enact provisions that will not put customers' lives at risk and avoid setting up a two-tiered system which targets low-income and minority customers.