

## IN THIS ISSUE

**“Over-Noticing” Service Disconnections  
for Nonpayment**

## NOTE TO READERS

## ON-LINE DELIVERY

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**OVER-NOTICING THE DISCONNECTION OF  
SERVICE DOES NOT SERVE, AND MAY IMPEDE,  
BILL COLLECTION OBJECTIVES**

Tacoma Public Utilities should make modest changes to its process of providing notices of the potential disconnection of service for nonpayment (DNP). In a report to TPU, FSC found that not only is the existing TPU disconnect notice process inconsistent with the stated objective of such notices, but the DNP notice process is likely even to be counter-productive to the prompt collection of unpaid bills.

**ARTICULATING THE OBJECTIVE OF SERVICE  
DISCONNECTIONS AND DISCONNECT NOTICES**

The objective of a service disconnection for nonpayment for Tacoma Public Utilities can be derived from the customer service regulations set forth in the Tacoma Municipal Code. According to the Municipal Code, if bills rendered to Tacoma utility customers “are not paid when due, they shall become delinquent, the Director shall, *if the same is necessary to enforce payment of said bills*, cause a discontinuance of service from the premises affected by such delinquency and service shall remain off until arrangement satisfactory to the Director has been made covering payment of the delinquent bill.” (emphasis added)<sup>1</sup>

The function of a DNP notice flows from this right to terminate service for nonpayment. According to the Tacoma Municipal Code, with unrelated exceptions, “termination of electric service to a premises. . . shall not occur until: (1) Tacoma Power has provided the customer reasonable notice of the intent to terminate electric service; and (2) the customer has been offered the opportunity of a hearing before a hearing officer.”<sup>2</sup>

<sup>1</sup> Tacoma Municipal Code, §12.06.110(B) (2009).

<sup>2</sup> Tacoma Municipal Code §12.06.115(E) (2009).

These sections of the Code make clear the objectives of the disconnect process. The disconnection of service is to occur if “necessary to enforce payment of [Tacoma utility] bills.” The disconnect notice is to notify the customer of the “intent to terminate electric service.” While the cited Municipal Code sections relate to electric bills, the policy statements would be equally applicable to other Tacoma utility services.

#### **THE SHORTCOMINGS OF THE TPU DISCONNECT NOTICE PROCESSES**

It is not uncommon for utility companies to send out shutoff notices when they have no intent to terminate service. Either the utility does not have the staff to effectuate a service discontinuance for each customer receiving a notice of discontinuance, or the company finds that it is not cost-effective to discontinue service for customers with arrears that are either less than some internally established “treatment amount” or younger than some internally-prescribed threshold.

#### ***Data from Other Utilities***

The actions of Public Service Company of New Mexico (PNM), for example, are typical of New Mexico utilities that over-notice service disconnections. A recent study by Fisher, Sheehan & Colton (FSC) examined the number of disconnect notices and the number of disconnections that PNM pursued for the years 2001 through 2007 (2007 reports only six months of data). The FSC review found that for the years 2001 through 2004, PNM issued between 20 and 25 disconnect notices for every one service disconnection for nonpayment the Company actually implemented. For the years 2005 through 2007 (mid-year), PNM issued more than ten notices for every service disconnection actually implemented.

FSC found a similar pattern in Ontario utilities providing data to the Ontario Energy Board in that Board’s review of low-income programs. Union Gas provided the most glaring example, with Hydro One close behind. From 2006

through 2008 (YTD), Union Gas printed shutoff notices on between 15 and 20 customer bills for every shutoff the company actually implemented. In the year with the *highest* follow-up (2006), only 7% of the Union Gas shutoff notices was actually followed-up by an actual disconnection of service.

Hydro One reported similar data. Between 2006 and 2008, Hydro One issued between 10 and 16 shutoff notices for each shutoff that the Company actually implemented. In the year with the highest follow-up, only 10% of Hydro One’s shutoff notices were followed-up with an actual disconnection of service. Toronto Hydro more narrowly targeted its disconnect notices, with a follow-up of close to 20% in 2006 and 2007; no 2008 data was reported by Toronto Hydro.

Only Enbridge Gas targeted its disconnect notices to customers it intends to actually disconnect, with a follow-up rate of between 80% and 85% for 2006 and 2007.

#### ***TPU Shutoff Notice Practices***

TPU staff, as well as the *Credit and Collections Guidelines* (2005), acknowledge that disconnect notices to customers with unpaid bills are computer-generated notices that are sent to all delinquent customers without respect to whether there is a current intent to actually disconnect service. According to the *Credit and Collections Guidelines*, there are two levels of a “disconnect notice” (as distinguished from a “Warning Bill”):

- a “Dunning Level 2” disconnect notice “is when the customer receives a notice from the utility that they (sic) are about to be disconnected if they don’t pay the past due amount. It is mailed 25 days after the due date of the original invoice. . .”
- a “Dunning Level 3” disconnect notice “is the actual disconnection notification that is sent to the Field Investigator to go to the premise and disconnect the service. The notification is created and sent to the field

32 days after the original due date of the invoice.”

As is evident from these Guidelines, issuance of the disconnect notices are driven by the time that has elapsed since the “original due date of the invoice.”

The disconnect notices, themselves, do not distinguish between whether the customer is, in fact, in imminent danger of disconnection for nonpayment. The notice states: “This account must be brought up to date within 48 hours or services are subject to disconnection without further notice. A reconnection fee will be charged to restore service.”

The notice certainly does not provide completely accurate information on the payment that is required. For example, rather than being required to bring the account completely “up to date” to avoid service disconnection, the customer would, in fact, be required only to make sufficient payment to reduce the outstanding balance below the dunning amount.

The over-reliance of Tacoma Public Utilities on what it terms “delinquency notices” has been previously communicated to TPU. According to the June 2008 customer care and billing *Benchmarking Report* prepared by UtiliPoint International, “TPU sends a unusually high number of delinquency notices in relation to collections calls and outstanding balances.”

According to the UtiliPoint benchmarking report, TPU issues a average of 50,200 delinquency notices each month. This volume of delinquency notices is three times higher than the “small electric utility” used by UtiliPoint as a benchmarking comparison (17,724 delinquency notices each month), and five times higher than the “reference group average” (10,762 delinquency notices each month) in the benchmarking study.

The problem with automatically sending computer-generated “shutoff notices” at a prescribed time after the due date on a bill is that not all

delinquent bills are subject to the disconnection of service. TPU has established dunning thresholds for the collection of accounts. For residential bi-monthly bills, balances of between \$200 and \$400, for example, receive a disconnect notice 25 days after the original due date, but no field notice is generated. For residential monthly bills, accounts with a balance of between \$70 and \$100 receive a disconnect notice 25 days after the original due date, but no field notice is generated.

#### **THE LAW GOVERNING OVER-NOTICING OF SERVICE DISCONNECTIONS FOR NONPAYMENT**

Aside from the unlawful nature of threatening collection activities when no present intent exists to engage in those activities, the provision of a notice of a service discontinuance when there is no present intent to engage in the discontinuance is counterproductive to the entire purpose of notice with which to begin. The purpose of a notice is to provide a clear and believable warning that a service termination is about to occur. In response to such a notice, the customer must either take the steps necessary to prevent the service termination or take those steps needed to protect himself or herself against the dangers to life, health and property that might result from the loss of service.

As can be seen, TPU appears to have fallen into the same trap as did Columbia Gas Company, an Ohio utility whose disconnect notice policies were challenged in federal court.<sup>3</sup> In rejecting the reasonableness of the notices of that Ohio utility, the court found that the company issued between 120,000 and 140,000 notices per year, only about 4% of which were followed by actual terminations. The Federal Circuit Court held that “it is clear that the flood of final notices sent out by the company was, as the District Court expressed it, “a wolf kind of notice” which does not conform to the constitutional requirements

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<sup>3</sup> *Palmer v. Columbia Gas*, 479 F.2d 153 (6<sup>th</sup> Cir. 1973).

that notice be truly informative and be given at a meaningful time.”

The purpose of this reference to the Columbia Gas court decision is to urge that, as found by the *Palmer* court, the repeated issuance of notices does not conform to requirements that notices be truly informative and be given at a meaningful time. As the *Palmer* court noted: “what we have here is a wolf kind of notice that is very convenient for the computer to issue, but is not, I think, what the statute contemplates, which. . . is a meaningful notice that applies to the person who is going to be affected by it and will be followed by some action.”

In TPU’s situation, it is not a “statute” that provides the reference point. Rather, it is the municipal code that provides that disconnections are only to be implemented when necessary to enforce the payment of bills. Disconnect notices are to be issued to convey the intent to disconnect service.

#### **THE BUSINESS COST OF OVER-NOTICING OF SERVICE DISCONNECTIONS FOR NONPAYMENT**

Aside from the legal implications of threatening the termination of service when no present intent exists to implement such disconnection, FSC told TPU that it should be aware of the business cost to issuing empty collection threats as well. A study by the New York Public Service Commission staff, for example, reported that:

The effectiveness of Final Termination Notices as a means to encourage payments or to make payment arrangements prior to field action has deteriorated. The rate of customer non-responses to Final Termination Notices has increased from 33% in 1983 to 46% in 1987. This may result in part from customer perception that utilities threaten to terminate service, but rarely do. In 1983, 16% of the customers who did not make arrangements on their arrears in response to a termination notice had their service terminated; in 1987,

only 9% of those customers had their service terminated.<sup>4</sup>

While the New York report is somewhat dated, FSC said, its conclusions are timeless. When a utility repeatedly issues shutoff notices warning customers of an imminent pending service disconnection unless bills are paid in full, without following up those notices by performing the threatened collection activity, it conveys the message that customers may ignore the shutoff notice with no adverse result arising.

#### **RECOMMENDED REFORMS OF PROCESS OF PROVIDING DISCONNECT NOTICES**

FSC’s analysis of TPU disconnect processes concluded that that utility should adopt the following policies with respect to the issuance of notices regarding the potential disconnections for nonpayment:

- TPU will not threaten to terminate service when it has no present intent to terminate service or when actual termination is prohibited by law. Notice of the intent to terminate will be used only as a warning that service will in fact be terminated in accordance with stated TPU procedures, unless the ratepayer or occupant remedies the situation which gave rise to the enforcement efforts of the utility.
- TPU will issue every notice of a pending disconnection of service for nonpayment at a meaningful time and in a meaningful manner. To meet this standard, a TPU shutoff notice will contain the following specific information and meet the following specific standards (1) a TPU shutoff notice will state the reasons for having the utility seek the termination of service; (2) a TPU shutoff notice will give a clear and believable warning that termination is

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<sup>4</sup> David Sawyer and Phillip Teumin, *Gas and Power Utility Uncollectibles and Collection Activity*, A Report by the Consumers Services Division of the New York State Public Service Commission.

about to occur; and (3) a TPU notice will fully inform the consumer of the required procedure by which the proposed termination can be avoided.<sup>5</sup>

- TPU shall not make a practice of delivering more than two consecutive notices of discontinuance for past due bills without engaging in the collection identified in the notice absent bill payment by the customer.

### ***Low-Income “Holds” on Service Disconnections***

In addition, FSC found that TPU would improve its internal finances through certain reforms to its disconnect process. For example, FSC noted, most utilities argue that the disconnection of service is a collection tool to be used to minimize uncollectible accounts. The assumption behind this argument (often unstated) is that the disconnection of service leads to the least-cost provision of service to remaining, paying, customers.

FSC found, however, that even if the premise of this argument is true (that the disconnection of service is an effective collection tool), the conclusion (that service disconnections result in least-cost service) does not necessarily follow.

### **The Implicit as well as Explicit Costs of Disconnecting Service for Nonpayment**

The disconnection of service yields both implicit and explicit costs to the utility. Perhaps the most notable explicit costs is the loss of revenue due to bad debt. When customers are removed from the system, TPU tends to lose the majority of dollars that represented the outstanding arrears. When customers have received their final bill and been removed from the TPU system,

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<sup>5</sup> In this respect, informing customers that their only option to avoid the disconnection of service is to pay the “full” bill, when, in fact, payment of a lesser amount that would bring a balance below the dunning level is not only misleading and deceptive, it places at risk receiving partial payments by the utility.

they are ultimately referred to collections for further processing. In 2007, the utility referred \$2.4 million to its collection agency. The agency collected \$740,000 (31%), of which \$120,000 was kept by the agency as fees (resulting in a 26% collection rate for TPU). In 2008, TPU referred \$2.4 million to its collection agency. The agency collected \$1.1 million (42%), of which roughly \$140,000 was kept in fees (resulting in a 36% collection rate for TPU).

In addition to out-of-pocket lost revenue experienced by TPU, the utility, of course, also lost the expenses associated with the carrying costs of the revenue assigned to collections, the expenses associated with the staff collection activity and customer services directed toward those accounts, and the opportunity costs associated with addressing the nonpayment by these customers rather than other payment-troubled customers.

The implicit costs are substantial as well. With low-income customers, in particular, the costs of disconnecting service are even higher than the costs associated with non-low-income customers. This is true when there is a fee designed to pass on the cost of the disconnect/reconnect process to the affected household as well as when there is not. Even when the cost of disconnection and reconnection is fully recovered from the nonpaying low-income household, that fee tends to divert limited household funds from the payment of current usage to the payment of the costs of the collection process, to the detriment of all involved.

A utility does not benefit its “paying” ratepayers if, through the disconnection process, it *increases* the unpaid debt of the disconnected household. In the event that a customer makes no payment toward her outstanding arrears, the utility goes uncompensated for both the initial arrears plus the uncompensated cost of the disconnection process. All the utility has thus accomplished through the disconnection process in this case, therefore, is to increase the loss to remaining ratepayers.

Even assuming that the disconnect/reconnect process is paid for through disconnect/reconnect fees, a household which is not permanently removed from the system, but which instead merely has its service disconnected and reconnected, ends up necessarily owing *more* than the arrears underlying the disconnection in the first instance. At the time of reconnection, in other words, in addition to the arrears which led to the disconnection, the household is responsible also for paying any disconnect and reconnect fee. Because of these additional payment obligations, when the household is poor, everyone loses.

As with the partial payment, given this information, the question which TPU must face is whether, by increasing the total outstanding bill owed by the low-income household, the utility is in effect diverting scarce household resources from the payment of current monthly bills to other expenses. If indeed this is the case, and if indeed the household has a limited amount of money that can be devoted to its utility bill, the presence of a \$60 fee for a disconnect/reconnect expense can only have the impact of putting future payments toward current monthly bills at greater risk.

### **The Recommended Change in Low-Income Disconnect Procedures**

Tacoma Public Utilities should adopt a 30-day “hold” provision for customers that it has identified through its Early Identification Program as likely being low-income.

The 30-day hold provision could, for example, be based on the regulations of the Iowa Utility Board (IUB). IUB regulations provide that “if the utility is informed that the customer’s household may qualify for winter energy assistance or weatherization funds, *there shall be no disconnection of service* for 30 days from the date the utility is notified to allow the customer time to obtain assistance.” (Iowa Admin. Code, §199-20.4(10)). (emphasis added). Postponing the disconnection of service is mandatory under the regulation.

Implementing a 30-day hold provision would allow reasonable time for TPU’s network of community-based organizations to undertake the process by which to determine whether the customer is eligible for public assistance. Public assistance may come in the form of energy assistance toward current bills, energy assistance directed toward arrears, TPU’s low-income discount, or other public and private income-supplements. Allowing the 30-day hold for customers identified in the TPU customer information system (CIS) as being “low-income” will lessen the likelihood that the customer will be found ineligible for assistance.

Allowing the 30-day hold presents a least-cost mechanism for obtaining payment of an outstanding utility bill. The implementation of a 30-day hold provision does not impose either the explicit costs or the implicit costs identified above as arising from pursuit of the service disconnection process.

Moreover, allowing such a 30-day hold is most consistent with the objective articulated in the Tacoma Municipal Code. As noted above, the Municipal Code provides that the disconnection of service is to occur *only* when such service termination “is necessary to enforce payment of said bills. . .” If a customer is identified in the CIS as likely being low-income, the availability of public assistance makes it more likely that the outstanding bill can be paid without resort to a service disconnection.

### **SUMMARY AND CONCLUSIONS**

In the world of collections, more is not always better. With utility collections in particular, several tests should be applied to determine the propriety of utility dunning activities. Whether a utility collection practice is effective is but one question in the analysis. Whether the utility collection practice is cost-effective, as well as whether the practice is efficient in operation, present further tests to apply.

FSC concluded that TPU should modify its disconnect process to improve the effectiveness, cost-effectiveness and efficiency of its existing termination notice processes. In particular, TPU tends to over-notice the disconnection of service. When TPU routinely provides a notice of its “intent to disconnect” service so many times, with no follow-up activity, payment-troubled customers learn that they need not pay particular attention to the receipt of a shutoff notice. As one Ohio utility’s shutoff notices were described, the computer-generated shutoff notice that does not presage the collection action communicated in the notice becomes a “wolf type” of warning.

FSC further concluded that TPU should modify its disconnect notice process. TPU notices of disconnection should provide clear and believable warnings of the imminent disconnection of service should payment not be made. Moreover, the utility should notify customer not only of the need for full performance, but of what payment performance is required to prevent further dunning activity.

FSC finally concluded that TPU should emulate the customer service regulations of other states in providing a “hold” provision for customers identified as “low-income” (which identification is recommended and discussed elsewhere). This “hold” process allows an identified low-income customer to apply for and receive a determination of eligibility for public and private assistance that might resolve the customer’s payment emergency. The “hold” process not only makes it more likely that an unpaid low-income will be retired, but also it makes it less likely that the bill will be retired only after expensive and increasingly intense dunning activities.

For help in assessing the propriety of the disconnect process in a particular state, or for a particular utility, contact:

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Fisher, Sheehan and Colton, Public Finance and General Economics (FSC) provides economic, financial and regulatory consulting. The areas in which FSC has worked include energy law and economics, fair housing, affordable housing development, local planning and zoning, energy efficiency planning, community economic development, poverty and telecommunications policy, regulatory economics, and public welfare policy.