

STATE OF NEW YORK  
PUBLIC SERVICE COMMISSION

Proceeding on the Motion of the Commission	)	
To Assess Certain Aspects of the Residential and	)	Case 12-M-0476
Small Non-residential Retail Energy Markets in	)	
New York State	)	
In the Matter of Retail Access Business Rules	)	Case 98-M-1343
In the Matter of Energy Service Company Price Reporting	)	Case 06-M-0647
Requirements	)	

**COMMENT OF THE STAFF OF THE FEDERAL TRADE COMMISSION<sup>1</sup>**

January 24, 2013

**I. Introduction**

The Federal Trade Commission (FTC) staff appreciates this opportunity to respond to the State of New York Public Service Commission's (NY PSC's) Notice Seeking Comments (Notice).<sup>2</sup> The notice seeks input concerning the NY PSC's review of competition and consumer protection rules in retail energy markets in New York State. We commend the NY PSC for its efforts to make retail electricity markets more beneficial for consumers through appropriate consumer protection provisions and effective competition. This comment draws on the FTC's

Many of the challenges that the NY PSC is considering require not only ensuring the disclosure of useful information, but also making such disclosures easy for consumers to understand and use to make informed decisions. The FTC uses pre-sale information disclosure requirements and law enforcement to improve the clarity of information about pricing and product characteristics such as energy efficiency. Mandated disclosures are more helpful to consumers if they present relevant facts and use plain language and graphics that are easy to interpret correctly. In Section III, we encourage the NY PSC to consider employing consumer education and communications experts and quantitative, controlled consumer testing where feasible. The FTC finds these tools valuable in designing effective disclosures.

In Section IV, we emphasize that consumers are likely to need easy-to-use tools to understand some of the complex disclosures that the NY PSC contemplates. In conjunction with voluntary disclosures, such tools have the potential to change market outcomes. In particular, Section IV discusses the usefulness of a calculator website that could facilitate customers' ability to compare prices and features of competing offers.

Carefully designed consumer protection policies often can achieve their goals without reducing or distorting competition. We are concerned that implementation of some of the ideas on which the NY PSC requests comments might di

efforts.<sup>5</sup> The FTC's competition advocacy program has produced two staff reports on electric power industry restructuring issues at the wholesale and retail levels.<sup>6</sup> The FTC staff also contributed to the work of the Electric Energy Market Competition Task Force, which issued a *Report to Congress* in the spring of 2007 (available at <http://www.ferc.gov/legal/fed-sta/ene-pol-act/epact-final-rpt.pdf>).

The FTC designs numerous energy cost disclosures, including the EnergyGuide label for appliances<sup>7</sup> and light bulbs,<sup>8</sup> and has done consumer research in support of those label-design efforts.

The FTC and its staff have filed numerous comments advocating competition and consumer protection principles with state utility commissions, state legislatures, professional organizations, the Federal Communications Commission (FCC), and the Federal Energy Regulatory Commission.<sup>9</sup> The FTC provided comments to the FCC on policies to reduce “cramming” – the placement of unauthorized charges on consumers’ phone bills.<sup>10</sup> The FTC also offers comments

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<sup>5</sup> *See, e.g.*

to state policymakers in support of policies that benefit consumers by allowing competition.<sup>11</sup> Other FTC comments have discussed how various policies – including restrictions on advertising – can harm consumers by reducing competition.<sup>12</sup> FTC comments have pointed out that competition-reducing policies often are neither necessary nor effective to protect consumers.<sup>13</sup>

### **III. Careful Analysis of Tradeoffs in Disclosure Design – Coupled with the Recognition that Significant Technological Change Is Possible – Can Benefit Consumers**

Simple, well-designed disclosures can help consumers make informed choices. Developing disclosures benefits from careful thinking about existing and future product offerings, expertise in consumer education and communications, rigorous testing, and confronting tradeoffs between simplicity and flexibility. Carefully designed policies that can accommodate the diversity of existing and future electricity offerings are likely to serve consumers better than policies closely focused only on the most common existing electricity offerings. In the longer term, home automation and smart grid technologies may lead ESCOs to increase product diversity. Terse disclosures are necessary oversimplifications of complex offerings in retail energy markets. Adding too many details to disclosures can confuse consumers and distract them from the more pertinent material. The FTC often uses controlled, quantitative comprehension testing to assess and improve the information that a disclosure conveys to consumers. Among other things, consumer testing can illuminate whether the benefits of disclosing non-price differences among

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Format (CC Docket No. 98-170), *available at* <http://www.ftc.gov/os/2011/12/111227crammingcomment.pdf> and <http://www.ftc.gov/os/2012/07/120723crammingcomment.pdf>.

<sup>11</sup> *See, e.g.*, FTC Staff Letter to Hon. Stephen LaRoque, North Carolina House of Representatives, Concerning North Carolina House Bill 698 and the Regulation of Dental Service Organizations and the Business Organization of Dental Practices in North Carolina (May 25, 2012), *available at* <http://www.ftc.gov/os/2012/05/1205ncdental.pdf>; FTC and U.S. Department of Justice Comments to Hon. Helene E. Weinstein Regarding New York Assembly Bill A05596 (To Establish that Certain Services Related to Real Estate Transactions May Be Provided Only by Attorneys) (June 21, 2006), *available at* <http://www.ftc.gov/os/2006/06/V060016NYUplFinal.pdf>.

<sup>12</sup> *See, e.g.*, FTC Staff Comment Before the Professional Ethics Committee for the State Bar of Texas Regarding Online Attorney Matching Programs (May 26, 2006), *available at* <http://www.ftc.gov/os/2006/05/V060017CommentsonaRequestforAnEthicsOpinionImage.pdf>.

<sup>13</sup> *See, e.g.*, FTC Staff Comment to Hon. Noble E. Ellington Concerning Louisiana Senate Bill 642 (To Define More Clearly the Type of Seller that Must Be Licensed as an Auctioneer) (May 26, 2006), *available at* <http://www.ftc.gov/os/2006/06/VO60015CommentstoLouisianaStateSenateImage.pdf> (“it is unlikely that requiring TAs [trading assistants, who help people sell products on online-auction sites] to become licensed auctioneers or licensed auction businesses will address the most serious fraud-driven consumer complaints associated with Internet auctions”).

ESCO offerings (such as environmental benefits and early termination charges) outweigh any confusion that such disclosures may cause.

Notice items 2 and 12 prompt this discussion. For instance, item 2 asks whether utilities should “include a line item on ESCO customer bills that identifies what the customer would have paid had supply been purchased from the utility.”<sup>14</sup>

A practical goal of retail electricity regulation is to help customers make informed choices in a way that does not distort or undercut effective competition. When each New York customer receives an electric bill from the utility that owns the distribution grid in the customer’s area, that bill may contain charges from the ESCO the customer has chosen to provide energy. Item 2 would remind ESCO customers – but not customers of the incumbent utility – that they can shop for competitors. It would notify ESCO customers – but not the incumbent’s customers – about whether a stable, reputable company offers a lower price. Competition works best when there is a level playing field and when all consumers have ready access to relevant information. The asymmetric approach described in Notice item 2 may tilt rather than level the competitive playing field.

It may be helpful to have disclosures comparing the commodity electric service offerings that currently dominate the market against a benchmark, but the rule may serve customers best if it covers the likelihood that quite different types of service will enter the market. If retail electricity service varies little among suppliers, then comparing a retailer’s price to an appropriate benchmark could motivate customers who are not buying from a low-cost supplier to seek better alternatives. At the moment, much of retail electric service is sufficiently undifferentiated that academics consider it reasonable to view the lowest-cost supplier as the best choice for the consumer and to study whether consumers are buying from that supplier.<sup>15</sup> Because it may cost more than comparable services, however, the standard default service price may not be the best alternative on which to focus a customer’s attention.

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<sup>14</sup> It may be more helpful to show what the consumer would have paid over the prior year than over the prior month, since variable pricing could save the consumer money on an annual basis despite looking worse during peak-priced months. Uri Gneezy and Jan Potters show that presenting information on periods that are too short can reduce willingness to take risks and distort choices. U. Gneezy and J. Potters, “An Experiment on Risk Taking and Evaluation Periods,” 112:2 Q.J. Econ. 631 (1997).

<sup>15</sup> Catherine Waddams Price, “Spoilt for Choice? The Costs and Benefits of Opening UK Residential Energy Markets,” Univ. of Cal. Energy Inst., Center for Study of Energy Markets, Working Paper 123 (2004), available at <http://www.ucei.berkeley.edu/PDF/csemwp123.pdf>; Ali Hortacsu, Seyed Ali Madanizadeh, and Steve Puller, “Power to Choose: An Analysis of Consumer Behavior in the Texas Retail Electric Market,” available at [http://www.ftc.gov/be/workshops/microeconomics/2010/docs/puller\\_slide.pdf](http://www.ftc.gov/be/workshops/microeconomics/2010/docs/puller_slide.pdf).

Even with existing technologies, the careful design of disclosures may be necessary to appropriately accommodate differences in offers to customers, such as early termination fees<sup>16</sup> and green power offerings. Price comparisons that disclose \$10 per month in savings – but not a far larger termination fee – could lead customers to make penny-wise but pound-foolish choices. Price disclosures for plans with early termination fees might be particularly valuable at the enrollment stage, at early post-enrollment, and at renewal. Similarly, requiring the bill of a customer who buys green power from an ESCO to disclose only the incumbent utility’s price for conventional power would not reveal whether the customer is getting a competitive price on green power. It might be appropriate to disclose a green power benchmark price to customers of green ESCOs in addition to disclosing the price for the standard default service. Moreover, policies may need to be flexible enough to accommodate the new kinds of offerings that ESCOs will create in response to any new disclosure or re-enrollment rules that the NY PSC adopts. Further, it is important to note that retail electricity offerings appear to be evolving toward more varied service characteristics, promotional incentives, and prices. Disclosures in the future will need to provide consumers with information sufficient to analyze whether these differentiated products are appealing at their stated prices.

Technological change is likely to differentiate services further. In coming years, the NY PSC may consider investments in technologies that will allow power retailers to market differentiated home automation and smart grid services and customer experiences. Meanwhile, telecommunications, home security, and technology companies already are offering smart home energy management services that operate primarily on the customer side of the meter. For example, advances in technology likely will allow power retailers to offer customers ways to save money by shifting consumption (such as electric vehicle recharging) to off-peak hours and empower customers to manage their energy use (and their home security systems) through a

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<sup>16</sup> ESCOs that supply home-automation hardware and price this cost into their monthly charges are likely to use early termination fees to ensure that the customer pays for the hardware. In the context of what ESCOs should have to prove to justify termination fees, such equipment or services could serve to justify termination fees equal to the value of the equipment.

Another legitimate business justification for termination fees may arise when ESCOs offer fixed-price electricity or price hedges during periods of volatile wholesale prices. Without the termination charges in these situations, customers could free-ride on the ESCO’s price insurance purchase by accepting the fixed retail contract when wholesale prices might be high, and then dropping out when they learn that wholesale prices will be low. That would be a “heads the customer wins, tails the ESCO loses” situation. In this circumstance, the inability to create an early termination provision might cause ESCOs to stop offering fixed-price supply contracts or might force prices up for this type of service in that market.

Although these justifications are consistent with legitimate business reasons, early termination fees may still concern consumer protection authorities. Specifically, firms might find such fees profitable when the fees are poorly disclosed, when customers underestimate the likelihood that they will terminate and pay a fee, or when the fees discourage customers from switching to lower-priced ESCOs.

smart phone. These technologies already are rolling out – notably in Texas,<sup>17</sup> which has both retail electricity competition and wide deployment of smart meters. The new services also are being offered through home monitoring and control services from telecommunications companies.<sup>18</sup>

Rules designed to protect consumers in markets for homogeneous products may confuse or distract consumers of highly differentiated smart-grid-enabled energy services. A bill that includes both power and a suite of home automation tools is fundamentally different from a simple bill for commodity power service. Comparing those two bills might be no more informative than comparing the cost of a smart phone to the cost of making the same calls on a barebones landline – essentially an apples-to-oranges comparison. The smart phone and the smart grid products both are fundamentally more advanced than their predecessors.

Further, smart-grid-enabled electricity service likely will offer personalized tips and programmable thermostats that help people save energy. These tools may cost more per kilowatt-hour but will enable consumers to buy fewer kilowatt-hours. Disclosures that focus on the higher cost per unit without also estimating the savings from increased efficiency are one-sided and may mislead consumers. There will therefore be flaws in any disclosure that is based on the faulty premise that consumers will use the same amount of power regardless of whether they choose smart services.<sup>19</sup> Rules that result in confusing or irrelevant information about these products might be worse than simply exempting consumers of smart-grid-enabled service from the conventional power disclosure.

These points indicate that careful policy analysis must underpin decisions about whether to require a disclosure and what it should include. In order to identify what to disclose, policymakers need clear ideas about what constitutes a reasonable choice and what information customers would need to make such a choice. For example, the goal may be to equip a customer to identify low-cost providers of the kind of power the customer prefers. Testing proposed disclosures on representative samples of customers can help inform policymakers' views about what (and how) to disclose.

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<sup>17</sup> For example, Reliant (a competitive retailer in Texas) bundles a free, smart-phone-enabled Nest thermostat with its Learn and Conserve plan. *See* [http://www.reliant.com/en\\_US/Page/Shop/Public/misc\\_Nest\\_LandingPage\\_May2012.jsp?customer=New&txtPromocode=WR0505&stop\\_mobi=yes](http://www.reliant.com/en_US/Page/Shop/Public/misc_Nest_LandingPage_May2012.jsp?customer=New&txtPromocode=WR0505&stop_mobi=yes).

The FTC, which designs and mandates disclosure





Linguistics about how to write and design for audiences with low literacy levels and limited English proficiency.<sup>26</sup> If the NY PSC develops a disclosure and demonstrates that it helps customers understand whether they are getting a good deal, there seems to be significant value in providing that information to all customers. If the NY PSC can develop a helpful, easy-to-use disclosure, it seems worth including it on all bills so long as the benefits outweigh the costs of universal distribution.

#### **IV. Consumers May Need Calculator Websites to Understand Some of the Disclosures that the NY PSC Contemplates; Disclosures Can Change Incentives and Market Outcomes**

The Notice contemplates requiring the publication of rate formulas and other potentially complicated information. Informing customers to enable them to make better choices requires not merely disclosure of the pertinent facts but also a presentation that consumers find easy to understand. The NY PSC may wish to consider policies that foster not only rate formula disclosures but also the development of a calculator that facilitates customer pricing comparisons among the documented offerings. Although it seems important for the policy to lay the groundwork for an easy-to-use comparison website, actual mandates may not be necessary. Tools that make it easy for customers to identify attractive, transparent offers might encourage companies to offer such rates and let consumers choose them.

The NY PSC's retail choice website, <http://www.newyorkpowertochoose.com>, is an important disclosure tool. Nonetheless, our review of 12 variable rate offerings in two utility service areas suggests that some ESCOs neither disclose the formulas they use to determine variable rates nor offer detailed information about the month-to-month prices those formulas produce. Moreover, the website appears to require scrutiny of several web pages to determine whether each ESCO made meaningful rate disclosures. It should be made easy for customers to know when a company fails to disclose enough about its variable rate formula for a customer to make a meaningful evaluation. The FTC has brought enforcement actions against firms that engage in pricing policies that are profitable because they hide consumer charges.<sup>27</sup>

In item 13 of its Notice, the NY PSC asks for feedback about whether it should mandate that “all [ESCO] variable rate methodologies . . . be based on specified formulas tied to publicly available information.” We suggest an alternative: to revise the data fields in the NY PSC's website so that customers can readily identify which ESCOs meaningfully disclose their variable rate formulas. The NY PSC need not solve all of the data collection and presentation problems

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<sup>26</sup> FTC staff comment to the CFPB, *supra* note 4.

<sup>27</sup> *See, e.g.*, FTC Press Release, “Juno Online Services Settles FTC Charges Over Internet Service Advertisements” (May 15, 2001), *available at* <http://www.ftc.gov/opa/2001/05/juno.shtm> (“‘These so called “free” Internet access offers were anything but,’ said Jodie Bernstein, Director of the FTC’s Bureau of Consumer Protection. ‘Information about fees was hidden in the fine print. The relevant conditions of any offer should be disclosed clearly and conspicuously so that consumers can make their purchases based on the facts.’”).

by itself. Policies that lead to the disclosure of actual prices or rate formulas in standard, machine-readable formats might let third parties develop user-friendly price comparison and calculator websites.

If the disclosures prove helpful, we suspect that most customers will choose transparent offers over opaque or poorly documented offers. ESCOs that want to promote their products to cost-conscious customers are likely to report their prices voluntarily to the comparison site. It is entirely possible that such a tool would be sufficient to change the market equilibrium and allow the majority of customers to make well-informed choices. For example, customers might find an offer priced at the New York Independent System Operator (NYISO) wholesale price plus one percent to be extremely attractive relative to an opaque, poorly documented alternative.

A mandate to base rates on public price indexes is more likely to help consumers if it is accompanied by web calculators or other consumer-tested tools that offer simple, accurate explanations of the implications. Such a calculator would be consistent with, but likely broader than, the calculator mentioned in Notice item 1. These additional steps may also address the query in Notice item 5 about enhancing the “Power to Choose” website. For example, a consumer may not be equipped to compare rates based on a NYISO spot electricity price against rates based on a city gate natural gas price. It could be extremely helpful to consumers if a website allowed them to compare the bill implications of rate formulas by calculating hypothetical bills that show costs for each month in the calendar year. This may be particularly useful to consumers when one offer has a flat price per unit, while another has seasonal variations.

companies that overstated the energy benefits of their replacement windows.<sup>29</sup> These enforcement approaches may be relevant to the New York State retail energy markets as well.

monthly data on prices charged by ESCOs” or requiring ESCOs to “post all of their offerings on that [official, Power to Choose] website” (Notice item 5) could help reveal offers of commodity service that are so unattractive that they are likely to be sold only through questionable tactics. Requirements that make it easy to find such companies may facilitate investigation and enforcement activity and reduce the number of shadows in which unscrupulous companies can hide.

## VI. The Default Effects Literature Contains Findings Relevant to Item 12 in the Notice

In Item 12 of the Notice, the NY PSC asks about the implications of requiring “ESCOs to obtain affirmative consent from customers for contract renewals involving a change in price . . . [or] for all contract renewals.” The NY PSC’s question seems to include the possibility of returning customers to regulated, standard service even if the ESCO’s service is a better deal (*e.g.*, is still cheaper than the default service after the price change) or is differentiated (*e.g.*, is green or smart-grid-enabled). Customers who have limited time may make a rational decision not to respond to what they believe to be “junk” mail asking them to re-enroll. Requiring ESCOs to get affirmative assent to a price decrease may often be a waste of customers’ time. Requiring affirmative assent for a price change could discourage an ESCO from cutting prices or from offering a competitive price that it might need to raise later if market conditions change. Thus, this regulatory approach could have particularly troubling consequences in the not infrequent periods when average wholesale fuel or electric prices are changing significantly.

Item 12 could have the effect of driving customers back to utility service. Evidence from multiple recent studies that compare similarly situated consumers who face different defaults shows that a large number of consumers – often 50 percent or more – stay with the default decision.<sup>36</sup> Madrian and Shea find that a group of people who faced an opt-out decision about 401(k) enrollment had a participation rate 48.5 percent higher than a comparable opt-in group.<sup>37</sup> These findings have prompted scholars to suggest that policy designers can use the choice of defaults as a policy tool to “nudge” people toward a reasonable decision.<sup>38</sup>

Such a rule – requiring an opt-in to re-enroll – may create significant subscriber retention costs for ESCOs and send large numbers of customers back to standard service. This would likely make it significantly harder for ESCOs to retain consumers and, by raising their costs relative to those of the distribution utilities providing standard service, might undermine ESCOs’

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<sup>36</sup> For a review, *see* Stefano DellaVigna, “Psychology and Economics: Evidence from the Field,” 47:2 J. Econ. Lit. 315 (2009), *available at* <http://elsa.berkeley.edu/~sdellavi/wp/01-DellaVigna-4721.pdf> (esp. section 2.1.7 and note 11).

<sup>37</sup> Brigitte C. Madrian and Dennis F. Shea, “The Power of Suggestion: Inertia in 401(k) Participation and Savings Behavior,” 116 Q.J. Econ. 1149 (2001).

<sup>38</sup> *See* C. Camerer *et al.*, “Regulation for Conservatives: Behavioral Economics and the Case for ‘Asymmetric Paternalism,’” 151 U. Penn. L. Rev. 1211 (2003); RICHARD H. THALER & CASS R. SUNSTEIN, *NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH, AND HAPPINESS* (2008).

ability to provide more value than the standard service.<sup>39</sup> The FTC is on record opposing similar decisions that create an uneven playing field in other markets because such rules tend to harm consumers by distorting competition and creating inefficiencies.<sup>40</sup> Although such a rule could benefit customers whom ESCOs recruited through questionable marketing practices, appropriate law enforcement is an alternative – and potentially better targeted – way to minimize harm from unscrupulous marketing practices.

Forcing ESCOs to obtain affirmative re-enrollments only if they raise prices might discourage ESCOs from attempting to exploit inattentive customers by raising renewal prices. Such a rule, however, might encourage ESCOs instead to seek to profit from customer inattention by offering attractive, initial, “teaser” rates that increase before the time for contract renewal. ESCOs already offer introductory rates in New York. At the same time, such introductory discounts may be more beneficial to consumers than an equivalent amount of paid advertising, and they are certainly better for consumers than an identical offer without the discount.

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<sup>39</sup> Further, customer inertia partially blinds opt-in and opt-out decision processes, since people who want to stay with the default are indistinguishable from people who simply did not reply. An “active decision” approach that asks everyone to respond and indicate a preference distinguishes these groups and can yield informative data about what consumers prefer, but likely still needs a default decision rule in the background. See G. Carroll *et al.*, “Optimal Defaults and Active Decisions,” 124 Q.J. Econ. 1639 (2009).

<sup>40</sup> See, e.g., FTC Staff Comment to the Louisiana State Board of Dentistry Concerning Proposed Modifications to Louisiana’s Administrative Rules on the Practice of Portable and Mobile Dentistry (Dec. 18, 2009), available at <http://www.ftc.gov/os/2009/12/091224commentladentistry.pdf>. That comment reads in part: “We are concerned, however, that some of the proposed amendments discriminate between mobile [*i.e.*, often school-based] and office-based dentistry and restrict competition in an unnecessarily broad manner. . . . The largest potential barrier to mobile dentistry is found in proposed §313(G)(6), which would require dentists to conduct a separate meeting by telephone



