

## **Utilities Deal With Bad Debts By Selling Them**

NEW YORK -- Old-fashioned utilities may be staid, but at least they have guaranteed revenue, sparing them the ignominy wholesale power producers have faced.

Yet what happens when customers don't pay their bills? Then, even the relatively healthy utilities have financial ills.

Increasingly, the utilities' solution to bad debts is taking a page from the playbook of consumer-lending businesses: sell them.

With unemployment rising, more households are defaulting on bills, including such basics as utilities. That means missed payments, warning notices and eventually shutoffs. Severe winters and spikes in natural gas prices such as those seen two years ago add to the problem.

But utilities are discovering that even after collection attempts have failed, there's still money to be made from delinquent accounts. Companies that for years have been buying credit card, bank and auto debt are now buying utility debt as well, albeit at a considerable loss to the seller.

The discount may vary with the age of the receivable and geography, but most buyers pay utilities less than 10% of the amount owed, said Al Brothers, executive vice president of Cavalry Investments LLC, which has been buying utility debt for the last two years. Less than 5% of Cavalry's \$4.7 billion portfolio of receivables is utility-related, he said.

"The biggest issue we had to overcome was the perception that (utilities) would encounter a significant amount of negative publicity (by selling debt)," said Joel Lewis, president of Inovision, a unit of privately held Marlin Integrated Capital Holding Corp. Inovision has bought uncollected accounts from Duke Power, the regulated utility arm of Duke Energy Corp. (NYSE: DUK); PECO Energy Co. (NYSE: EXC); and First Energy .

Unlike credit-card companies, however, utilities have to worry about how delinquent customers will be treated by consumer debt buyers, Mr. Lewis said.

If customers believe they're not getting a fair shake from the new debt holder, they can file a complaint with the state public utilities commission, which can then take action against the utility.

"At worst, they can sue the utility company for selling unjust debt and the utility gets hung up in litigative action," Mr. Lewis explained.

He regards himself as the founder of the growing market. Five years ago, while debt manager for the utility units of Dominion Resources, he started to look for ways to increase collections. Inovision owns more than \$5 billion worth of debt, \$1 billion to \$1.25 billion of it utility-related.

PECO was one of the first utilities to sell its bad accounts. With 1.5 million electric and roughly 450,000 gas customers in southeastern Pennsylvania, PECO sold its first portfolio, with a face value of \$275,000, to Inovision in 1998. Since merging with Chicago holding company Unicom Corp. to form Exelon Corp., PECO continues to sell its bad debt.

Bruce Gay, former project manager for PECO's debt sales, says it's mostly residential and small commercial customer accounts that are sold, because large industrial customers' debt is viewed as "forever bad" and likely to end up in bankruptcy court.

While utilities often get just pennies on each dollar of debt sold, the returns are usually better when they don't wait as long to sell.

"Some utilities seem to be selling their paper earlier in the delinquency cycle, simply because they can get a higher price closer to the charge-off," said Mr. Gay, now president of Monticello Consulting Group Ltd. in Malvern, Pa. Charge-off accounts are those that have been written down to zero for accounting purposes, typically 180 days after the account is past due.

Commonwealth Edison, a Chicago utility owned by Exelon, has found that 12 months after charge-off is the optimal point for selling its bad accounts. Up until then the monthly returns on collection efforts outweigh the price it can get from a buyer, said Mark Falcone, director of revenue management for ComEd.

Duke Power, which began selling customer debt in 1997, said the practice is one way it's managed to maintain low electricity rates, at 1986 levels, according to company spokeswoman Paige Layne.

First Energy has been selling its unpaid electricity accounts in Pennsylvania and New Jersey only in the past few months, and is considering whether to sell uncollected debt in Ohio, spokesman Scott Surgeoner said.

Buyers for these accounts differ on what they're getting and what it's worth paying for, but there are some willing to buy even those accounts that appear hopeless.

For instance, Asset Acceptance Corp. prefers to buy utility accounts that have already been through three collection agencies and can be as much as two years old, initially because it's cheaper, says company president, Rufus "Bud" Rietzel. Asset Acceptance Corp. currently owns \$1.5 billion of utility paper, compared with about \$10 billion in other receivables, including home improvement loans and student loans.

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