



Energy Affordability and Energy Service Choices: Three Perspectives



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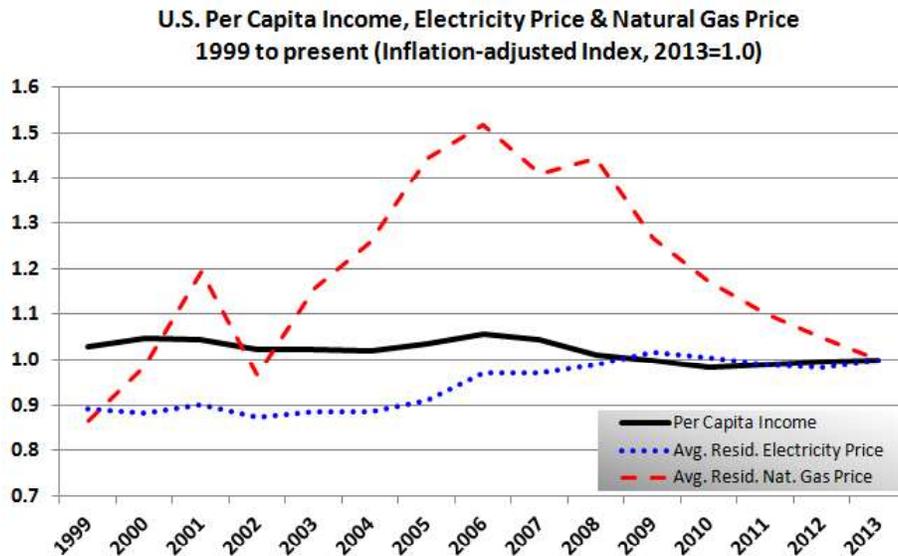
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Introduction

Many households find it challenging to afford basic needs, including energy, and recent macroeconomic trends have exacerbated the challenges they face. The average electricity price (revenues divided by sales) in the U.S. has been relatively stable recently, but it increased about 10% on an inflation-adjusted basis from 1999 to 2013. Natural gas prices have been much more volatile, and recently the average price has fallen from historic highs. However, the average price of natural gas to residential consumers in the U.S. has also risen by about 10% on an inflation-adjusted basis over that period. While these averages ignore regional variations in price, we can observe that for the nation as a whole, the cost of utility service has risen relative to the general level of inflation over the past 14 years.

Compounding the problem of affordability is a decrease in per capita income in the U.S. since 1999. The following chart tracks these three items—per capita income, average electric prices and average natural gas prices—in 15 annual snapshots. We know that the great recession reduced employment opportunities and wages for many families. This, coupled with reduced energy assistance funding, has made the affordability of energy a significant issue for low-income households.



Technical measures and average economic data do not provide a complete or satisfying story. There are great variations from state to state, and from one utility service territory to another. It is also important to discuss the qualitative aspects of energy affordability and the social and policy conditions that cause or perpetuate the problems. We want to improve our understanding of why low-income consumers cannot afford to pay their energy bills, what causes utility service to become less affordable, and what can be done to reverse these trends.

DEFG's Low Income Energy Issues Forum is focused on innovative and integrated policies and approaches that help close the widening gap between what vulnerable energy consumers can pay and their current utility bills. A diverse group of members has been meeting since early 2013. A recurring issue has been how to best meet the needs of individual customers and address the challenges of unique households. People find themselves in "situations" from time to time, and these situations are difficult to cope with. Some situations are temporary; the needs are short-lived; the problems are manageable with a small amount of bill assistance. Other people find themselves in deep holes with seemingly few exits. Government agencies, not-for-profit organizations and utilities cannot be all things to all people, but there may be new approaches that can help make energy more affordable to a greater number of people. The Low Income Energy Issues Forum is trying to identify these policies and approaches.

This white paper on energy affordability includes the perspectives of three experts: a low-income customer expert at an energy utility in Maryland, an executive at a not-for-profit energy assistance agency in Pennsylvania, and a former state utility commissioner from California.¹ Each author addresses several questions relating to energy affordability. This white paper is intended to supplement technical measures of energy affordability with some historical perspectives, a reflection on significant social and regulatory issues, and various points of view.

The following seven questions were posed to the authors:

1. What do you mean by “energy affordability”? How (if at all) is this term misused or misunderstood?
2. What is the current state of energy affordability in North America? Where can you note extremes (good or bad) related to energy affordability in North America (or the region you work in)? What conditions have played a role in the current state?
3. Consider the various segments of the population who have trouble paying their energy bills. Is it worthwhile identifying each of these segments and the conditions that led to their predicament?
4. Do you expect energy affordability to be an even more significant issue in five years? What factors are most important in determining the future state of energy affordability?
5. Given that different low-income consumers exhibit different preferences with regard to many aspects of utility service and uses of energy—for example, bill payment methods or channels of payment; patterns of appliance ownership and energy usage; preferences for more or less volatility in monthly bills and/or rates; frequency of contact with a utility call center, etc.—to what extent is a regulatory or utility “one-size-fits-all” tariff approach working for programs, services and rates? (For example, should utilities offer residential customers several different rate design options? Should more energy efficiency programs allow individual customization? Should service options be expanded to recognize the different ways that people choose to communicate or transact with the utility?)
6. What can or should utilities and regulatory agencies do to increase the choices (programs, services, rate options) available to each low-income energy consumer?
7. Can you provide examples of U.S. states and Canadian provinces which have replaced punitive policies and regulations (e.g., those which impose fees and penalties on low-income customers who do not behave like middle- and upper-income customers) with policies and/or regulations that encourage better payment performance by low-income consumers?

Question 1

What do you mean by “energy affordability”? How (if at all) is this term misused or misunderstood?

David Conn, Energy Assistance Program Manager, Baltimore Gas and Electric Company (BGE)

I would define “affordable” as a cost low enough to allow a household to pay for other basic needs, such as food, shelter, clothing and medical care. That’s the easy part. But how much should any given household have to spend on those basic needs?

Fisher, Sheehan & Colton have defined energy affordability as home energy that costs no more than 6% of a household’s gross income,² which is based on the U.S. Department of Housing and Urban Development’s standard that housing is unaffordable when it costs more than 30% of household income, and that home energy costs typically represent about 20% of shelter costs. However, APPRISE has argued in one study that home energy costs pose a high burden on low-

¹ Short author biographies appear in the appendix.

² In 2003, Fisher, Sheehan & Colton introduced a model to calculate the dollar amount by which actual home energy bills exceed affordable home energy bills on a county-by-county basis. See: <http://www.homeenergyaffordabilitygap.com/>

income households when they exceed 4.3% of income,³ and in another when they reach 11% of income.⁴ Those are averages, of course, and as a wise veteran legislator once warned me, you can drown in a swimming pool that's an *average* of one inch deep.

Obviously, there is no agreed upon figure that represents an exact affordable home energy cost, though most would agree that it must be defined relative to total household income. That's how most energy assistance programs determine eligibility and grant amounts—by comparing total energy costs to the household's total income, adjusted for the number of individuals in the household as a basic proxy for expenses.

Where I have concerns about this approach is that it ignores wide variations in household expenses. At BGE, and doubtless at utilities and social service agencies around the nation, we constantly try to address the needs of households who meet the assistance eligibility standards, but find the grants are often too small to resolve many customers' bill payment crises because they face substantial medical or other unavoidable costs that are not accounted for in eligibility formulas. Add in the higher costs of transportation, food and other vital needs for those living in low-income neighborhoods, and it's obvious why current assistance amounts leave so many families still in crisis.

As the National Regulatory Research Institute⁵ points out, without knowing the details of each customer's financial life, we can't know the hardships any customer faces in paying their utility bills, we can only know when they fail to do so.

Lastly, as the utility representative on this panel, I must point out that the price paid for energy does have to reflect the actual costs to produce and distribute it safely and reliably, along with a reasonable profit incentive for investors, to maintain and improve the system. A focus on affordability that ignores these basic economic facts is doomed to fail not only limited income households, but everyone who relies on energy—which, of course, is everyone.

Chad Quinn, Chief Executive Officer, Dollar Energy Fund, Pittsburgh

I believe that "energy affordability" is defined by the measure of expense, most often a percentage of a median income, which households can manage to maintain an adequate supply of home energy. This measure is created by assuming that households have everyday living expenses in line with others in their demographic segment. Typically, the percentage of ordinary monthly household income that can be used for energy is 6%.

Energy affordability is oftentimes misunderstood because it should not be a one size fits all approach. Many households, including those living slightly above the level typically referred to as low income, have a difficult time making ends meet. A safety net needs to be created to provide varying levels of assistance to "working poor" households experiencing financial hardships.

Timothy Alan Simon, Esq., Counsel and Consultant, TAS Strategies (former commissioner, California PUC)

From my perspective, energy affordability is the combined price of gas and electricity as a percentage of consumers spending within the context of the regional consumer price index. In electric markets, this should be differentiated between regulated cost-of-service, rate-of-return utilities, competitive electric marketers, government aggregators and municipal utilities.

³ "LIHEAP Energy Burden Evaluation Study: Final Report," Applied Public Policy Research Institute for Study and Evaluation (APPRISE), July 2005, p. iv. Available: <http://www.appriseinc.org/reports/LIHEAP%20BURDEN.pdf>

⁴ "Ratepayer-Funded Low-Income Energy Programs: Performance and Possibilities: Final Report," APPRISE and Fisher, Sheehan, and Colton, July 2007, p. iv. Available: <http://www.appriseinc.org/reports/NLIEC%20Multi-Sponsor%20Study.pdf>

⁵ "How to Determine the Effectiveness of Energy Assistance, and Why It's Important," Costello, NRRI, December 2009. Available: <http://www.nrri.org/web/guest/home> (search for "energy assistance")