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Prepayment Meters and Low-Income Consumers

Utility companies today are pushing to place more and more customers on meters that require customers to pay in advance. As the nation experiences dramatically increasing electric prices, however, it is particularly appropriate to consider the impacts that might be felt by low-income consumers that might be placed on prepayment meters.

FSC, in an article published by the American Bar Association, recently presented a detailed analysis of the impacts of prepayment meters on low-income consumers.

A prepayment meter operates through use of a plastic card. The consumer purchases a designated amount of energy from a local vendor which amount is then encoded on a magnetic strip on this card. The card is then inserted into the home electric meter which will operate until the purchased amount of energy is exhausted. At that time, all energy through the meter is blocked. Generally, prepayment meters will give a warning of from two to four days prior to the dollars being exhausted. "Cold weather protections" can be programmed into the meters. Prepayment meters can also be programmed to reflect differing rate blocks: flat, inclining or declining.

The consumer's card purchases might occur either at the utility company, or a local drug store, or any other utility pay station. Purchases might also be by mail. Existing prepayment meters provide for the purchase of electricity in blocks of dollars. A consumer, in other words, would purchase $50 of electricity rather than purchasing blocks of energy (*e.g.*, purchasing 500 kWh which happens to cost $x).

Utilities seeking to install prepayment meters generally seek approval for such meters as a credit and collection device. Under these circumstances, a prepayment meter will be promoted as a less intrusive alternative than the disconnection of service.

Payment Troubles and Low-Income Status

Prepayment meters used as a response to nonpayment will disproportionately affect low-income households. While it is accurate to say that bill payment troubles are not exclusively associated with low-income households, it not accurate to assert (or to imply) that payment troubles are unassociated with (or unrelated to) low-income status.

There is little question but that bill nonpayment disproportionately involves low-income consumers. One 1995 Census report, for example, found that while 9.8% of non-poor families could not pay their utility bills in full, 32.4% of poor families could not do so.

Moreover, according to the Census Bureau, while 1.8% of non-poor families had their electricity or natural gas disconnected for nonpayment, 8.5% of poor families suffered this same deprivation. This disconnection ratio increased even further for welfare recipients, to 10.5%. U.S. Census Bureau, ***Extended Measures of Well-Being: 1992***, P70-50RV (November 1995).

The significance is that it is grossly misleading to assert that a prepayment meter project will focus on payment-troubled customers, but to deny the notion that such a focus will necessarily disproportionately involve low-income customers.

This is particularly true if the program is administered primarily through a utility's customer service representatives. These representatives have their primary contacts with payment-troubled customers. In the event that it is those same personnel that will be responsible for enrolling participants in the prepayment program, those participants will come from a population that is heavily weighted toward low-income customers.

The Salt River Experience

The Salt River Project in Arizona, which is often held up as an example for other companies, is not a good precedent for companies who will serve primarily low-income consumers with prepayment meters. Indeed, the experience of the Salt River Project prepayment meter project is not comparable to, or applicable to, low-income households, as well as to the working poor, in other states.

SRP reports, for example, that the typical prepayment family served by that utility owns its own home (58 percent), the family income is $31,000 a year, and the head of the household tends to be under 35 years old. The average household consists of four people and has been an SRP customer for more than 10 years.

Most low-income customers around the nation have incomes substantially below $31,000. 100% of the federal Poverty Level for a household of four, for example, is only $17,650. Moreover, most low-income households are not homeowners. Nor do they have a length of tenure of 10 years.

Prepayment Meters and Energy Savings.

It is easy to create the image of people turning off lights, turning down thermostats, and taking other affirmative steps to control consumption by behavioral changes. The savings potential through such steps, however, is insufficient to predicate the introduction of an entirely new generation of meters based upon such savings.

In addition, it may be easy to create the image of a vast savings potential that would arise if low-income households only turned off "wasteful" appliances. However, it is not the number of new appliances, but rather the age, condition and energy efficiency of basic appliances, as well as the age, condition and efficiency of the housing structure itself, that drives low-income consumption levels.

Statements that prepayment meters will help low-income consumers better control their energy consumption by making the consumer more aware of energy use appear to ignore the nature of low-income energy usage. The largest uses of electricity in a low-income home are frequently, if not generally, driven by factors outside the ability of the consumer to control.

Self-Disconnection of Service

One adverse impact of prepayment meters involves the extent to which low-income customers will self-disconnect their utility service by failing to purchase additional energy when that energy becomes unaffordable. In this circumstance, the disconnection of service is not avoided, but rather merely "hidden" from regulatory, and public, oversight.

A self-disconnection occurs when, rather than having a utility disconnect service for nonpayment, a consumer's meter runs out of money and, because the consumer lacks the necessary resources, the consumer fails to purchase additional energy to keep the meter operating. As a result, the flow of electricity or natural gas into the housing unit stops.

Prepayment meters provide a substantial cause for concern about self-disconnections. Great Britain has more than four million customers that use prepayment meters. An August 1999 study by a national consumer organization in Great Britain reported that "the number of people having their electricity supplies cut off has declined dramatically in recent years, mainly because people are being offered prepayment meters as an alternative to disconnection."

In its 1999 study, titled *Final Demand*, however, Consumers' Association found that "while electricity disconnection levels may be falling, this does not mean that the problems that many people face in paying their bills have gone away. Many people with prepayment meters can't afford to "feed" them and are effectively self-disconnecting their electricity supplies."

The consumer organization reported that a third of gas customers surveyed had self-disconnected in the last year. Moreover, over one-quarter of electricity customers had run out of electricity in the last year. "If these figures were nationally representative, it could mean that around 428,100 gas and 926,000 electricity consumers were self-disconnecting last year."

Paying Unaffordable Bills

One of the real myths about low-income energy bills is that problems only arise when low-income households fall into payment trouble. The payment problems of low-income customers, however, and the self-disconnection that will occur as a result of prepayment meters tell not even half of the story of unaffordable home energy bills. Research from 1999 documented that nonpayment is not the only impact of inability-to-pay. In addition, because of unaffordable home energy bills, low-income consumers are forced to make unreasonable budget decisions between competing household necessities (*e.g.*, heat or eat), and be forced to engage in a wide variety of dangerous and/or unhealthy activities in an effort to keep paying their utility bills.

The Iowa State Department of Human Rights further documented the impacts of these unaffordable home energy bills. According to a study performed by that agency, recipients of federal fuel assistance in Iowa exhibited the following characteristics in the 1999/2000 winter heating season as a result of unaffordable home energy bills: Over 12 percent went without food to pay their home heating bill. Projected to the total participating LIHEAP population, that meant that about 7,600 low-income households (representing 20,000 Iowa citizens) went without food at times as a result of unaffordable home heating bills.
More than one-in-five of the Iowa LIHEAP recipients went without medical care to pay for heating bills. This included not seeking medical assistance when it was needed, not filling prescriptions for medicine when a doctor had prescribed it, and/or not taking prescription medicines in the dosage ordered by the doctor.

Almost 30 percent reported that they did not pay other bills, but did not elaborate as to which bills were not paid. In addition to not paying other bills, many low-income households incurred debt in order to pay both their home heating bills and other basic necessities: borrowed from friends and/or neighbors; used credit cards to pay for food and other necessities, or did not pay the heating bill.

Even if not resulting in self-disconnections of low-income households, the use of prepayment meters imposes substantial harms on low-income households while at the same time impeding the distribution of public assistance that would help to address, and redress, those harms.

"Voluntary" Prepayment Agreements and Economic Duress

Utilities often argue that the use of prepayment meters is limited to customers who "voluntarily" agree to the installation of such meters as a means through which to address payment troubles.

Prepayment meters offered as an alternative to the disconnection of service, used as a collection device, or offered to low-income payment-troubled customers, cannot be found to based on an informed and true "consent."

In the law, there is a doctrine referred to as economic duress. When economic duress is present, "consent" will be found not to have been freely given, but rather to have been coerced. Duress is considered to exist under circumstances that would impede, if not overcome, the party's exercise of his or her free will.

The potential loss of essential utility service as an alternative to a "consent" to a prepayment meter represents such economic duress.

Moreover, the loss of utility service not only denies essential households services such as heating and light, but is generally considered to render a housing unit uninhabitable as well. If the loss of utility service does not represent duress, the uninhabitability of the housing unit (alone or in combination with the loss of utility service) would.

The Rate Implications of Prepayment Meters

Any prepayment meter program that is adopted by state regulators should be accompanied by discounts provided to participants in the program. Discounts accompanying prepayment meters are justified on two different grounds.

First prepayment meter customers impose fewer costs on a utility system, which limited costs should be reflected in lower rates. Moreover, of those costs, that a company does continue to incur, the prepayment meter class will have no responsibility for causing those costs to be incurred.

Second, prepayment meters constitute a "lesser" service that should, accordingly, be accompanied by a lesser charge.

A recommendation for lower rates to customers using prepayment meters has nothing to do with charging below-cost rates.

Cost Causation

Customers on prepayment meters impose less of a cost on the utility and are thus entitled to lower rates as a result. Cost savings that will be realized by the utility will arise in a variety of areas. These will include, at a minimum, working capital reductions, bad debt reductions, credit and collection reductions, billing reductions, and reductions in related services.

The principle of cost causation serving as the basis for public utility rates has long been embedded in American regulatory law. If a customer class causes the utility to incur certain costs, that customer class should be responsible for paying those costs. If, in contrast, the customer class is not the class that causes a utility to incur particular costs, that customer class should *not* be responsible for paying the

costs.

Cost responsibility largely follows cost causation. Because prepayment meters will eliminate the line of cost causation between certain costs and the class of customers using prepayment meters, the cost responsibility should be eliminated as well. What that means is that these customers should receive a lower rate to reflect the lower level of costs.

The need to produce a lower rate is to reflect a change in cost-causation and responsibility. Whether or not a company's costs actually decrease, the customers who are using prepayment meters can no longer be said to be the customers who are causing the company to incur those costs. Accordingly, whatever costs still exist should be allocated to those customers causing the company to incur them in the first place and away from prepayment meter customers.

Lesser Service

There is no question but that a company using prepayment meters will impose a stricter payment requirement, and less payment flexibility, on customers using prepayment meters than it does on its customers using traditional billing.

Traditional billing does not result in the immediate pursuit of collections if a bill is not paid. All public utilities operate under what they call a "treatment amount." Under the treatment amount, the utility will undertake no collection activity until an arrears reaches a certain size or age (or a combination of the two).

Many companies, for example, will undertake no collection activity for bills less than 60-days overdue. Many companies will undertake no collection activity for arrears of less than $75 or $100. This payment flexibility is lost under the prepayment meter initiative. When the meter runs dry, service is discontinued.

Even aside from collection activities, most utilities have a different and higher treatment amount for service termination. Merely because a company might initiate the collection process, involving a set of notices, when a customer reaches an arrears of $100 and/or 90 days does not mean that the company will disconnect service for arrears of that size and age.

To be cost-justified, the company will limit its service termination process to arrears of much greater age and magnitude. Not all customers in arrears have their service disconnected. Not all customers receiving a disconnect notice have their service disconnected (even if no payment is made). In contrast, customers on prepayment meters will receive no such dispensation.

Prepayment meters impose substantial limitations on a customer's decisions regarding bill payments. Prepayment meters do not allow a customer to make short-term budget decisions on whether to delay payment of one bill in order to meet other household necessities. A company's own data on the aging of arrears, for example, will likely show that the vast majority of its arrears do not represent a risk of loss to the company. Few 30-day arrears become 60-day arrears. And even fewer 60-day arrears become 90-day arrears. In those instances, a customer's service is not placed in jeopardy under traditional billing.

With prepayment meters, however, the option is never provided to the customer to manage his or her money to address household necessities. When the meter runs dry, a payment must be made irrespective of other household financial necessities or service is effectively terminated. This requirement is not placed on other customers.

This lack of flexibility is a particular problem for low-income and low wage customers. Low-income and low wage customers live on or below the line of economic viability. Even at the low wage jobs (setting aside the low-income population for a moment), if the ten year old automobile a new muffler, or if the four-year old

child gets sick (requiring the parent to miss two or three days of work), there is no financial cushion.

Under traditional billing, these customers do not place their energy service in jeopardy because of a broken refrigerator or a childhood illness. Under the prepayment meter, they do.

Special Customer Charges

The installation of prepayment meters is often accompanied by a proposal to collect the cost of the new meter through imposition of a new and higher customer charge. Louisville Gas and Electric, for example, proposed a new customer charge of $7.50 per month ($90 per year).

Low-income customers, in particular, are not likely to be able to pay off their $90 a year in extra customer charge through energy savings, even assuming that energy savings can be generated.

In Louisville, FSC found that even if you accept that customers will experience the same 10% savings that SRP customers experienced – remember that the SRP prepayment meters were accompanied by substantial energy education efforts-- there will not be a $90 annual savings. In Louisville, the total annual electric consumption was estimated by the Company to be about 10,500 kWh per year. A 10% savings would thus be 1,050 kWh per year. At the rate of 5.4 cents per kWh, customers would save only $56.70 per year. They would thus be spending $90 to save $57.

Since low-income customers use only 85% the consumption that higher income customers use (see, FSC Insights, May/June 2001), they would be even worse off. They would have a consumption of 8,925 kWh (10,500 x .85). They would have a savings of 893 kWh given the SRP 10% conservation. At a rate of 5.4 cents per kWh, they would have an annual savings of $48.20. They would thus be spending $90 to gain a savings of $48.

Anyone wishing a copy of the FSC article providing the analysis of prepayment meters can find the article in the American Bar Association's *Journal of Affordable Housing and Community Development* (Volume 10, No. 3/Spring 2001), or can send a request to:

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