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WHY UTILITIES ARE NOT WELL-SUITED TO DELIVER RELIEF TO LOW- AND MODERATE-INCOME CONSUMERS IN A CLIMATE BILL

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Comprehensive climate change legislation is expected to include measures to mitigate the effects of higher energy-related prices on low- and moderate-income family budgets. Those higher energy prices play an important role in achieving efficient emissions reductions under a cap-and-trade system (or under a carbon tax), and they are an inevitable result of measures that limit the supply of fossil-fuel energy. However, it is not inevitable that consumers face undue hardship as a result, and there is a broad consensus among policymakers that steps should be taken to avoid such an outcome.

Even a modest 15 percent reduction in greenhouse-gas emissions would cost the poorest fifth of Americans an average of \$750 a year per household. These households have average annual incomes of only about \$15,000. Without relief to offset these higher costs, millions of households would be driven into poverty, and those who already are poor would become significantly poorer.

The most efficient way to prevent this from happening and to protect low- and moderate-income consumers is through a

¹ Martha Coven also made a significant contribution to this report

KEY FINDINGS

Giving climate revenues to utility companies is not a sound way to protect low- and moderate-income consumers from higher energy prices:

- Utilities do not routinely collect information on their customers' incomes. To identify customers with low incomes, utilities would have to be subsidized to build a costly administrative infrastructure that duplicates what public agencies already do.
- Many low-income consumers would likely be missed. The "Lifeline" telephone discount program, the only federal program that delivers assistance to low-income people through utilities, reaches just *one-third* of eligible households.
- Relief from increases in utility bills would fall far short of restoring families' purchasing power losses. Less than half the impact of climate legislation on low-income consumers' budgets will come from higher home energy prices.
- Reducing households' utility bills would likely reduce their incentive to conserve energy.
- There is no good way to allocate funds for low-income relief among the nation's thousands of utilities. The formulas that have been proposed to allocate funds among utilities – whether based on population, the amount of electricity delivered, or emissions – would shortchange utilities that serve a disproportionate share of low- and moderate-income consumers.
- Oversight of utilities varies widely from state to state, so it will be difficult to ensure that federal funds are used appropriately.

A far more effective way to assist consumers would be through a "climate rebate" that directly compensates families for their lost purchasing power.

“climate rebate,” which would directly compensate families for their purchasing power losses, using revenues from a cap-and-trade system or carbon tax.² But some industry groups and policymakers have proposed instead that funds be given to local utility companies to assist their lower-income customers.

While relying on utility companies may seem a reasonable option at first blush, since electricity bills are expected to rise under a climate change policy, this approach is unsound for several reasons.

1. Utility companies do not routinely collect information on their customers’ incomes.

Utility companies cannot easily identify which of their consumers have low incomes. All they generally know is which customers are facing shut-offs because they have not been able to pay their bills. But people facing shut-offs represent only a small fraction of the low-income customer base, and this group (those facing shut-offs) includes some higher-income customers as well. Some utilities know which customers receive vendor payments on their behalf from the Low Income Home Energy Assistance Program, but LIHEAP serves only a very modest share of the eligible low-income population; only about one in every six low-income households eligible for LIHEAP receives it.

To target assistance at lower-income customers, utility companies would therefore have to set up new bureaucracies to collect and audit income information. Covering the large costs of building an infrastructure at each utility company to gather and verify income information for millions of customers would require substantial government subsidies. Such subsidies would pay for an infrastructure that essentially duplicates what public agencies already do.

Making households of all income levels eligible for utility company assistance would avoid this particular difficulty. But that approach would spread the funds much more thinly across the population and make it far less likely that low- and moderate-income consumers would be adequately protected from higher prices.

2. Past experience suggests that utility company programs will miss large numbers of low-income consumers.

The only existing federal program that delivers assistance to low-income households through utility companies is the “Lifeline” telephone discount program, administered through local phone companies. The companies are encouraged to coordinate the Lifeline enrollment process with the enrollment processes for government-administered public benefits, but in practice, such coordination is infrequent. Even where it does occur, large numbers of eligible households (in many cases half or more) do not make the transition from participation in public programs to Lifeline participation. The result is that, nationwide, the Lifeline program reaches just *one-third* of eligible low-income households.³ Two of every three eligible low-income households are left out.

² To learn more about how a “climate rebate” would work, see www.cbpp.org/6-3-08climate-fact.htm.

³ See Matt Fiedler, “Lessons from the Telephone Lifeline Program,” Center on Budget and Policy Priorities, July 18, 2008, available at www.cbpp.org/7-18-08climate.htm.

In addition, utility company programs would miss the significant share of low-income households who do *not* pay utility bills directly because their utility costs are included in their rent and hence the bills are paid by their landlords. These households will need help paying higher rents, not higher utility bills.

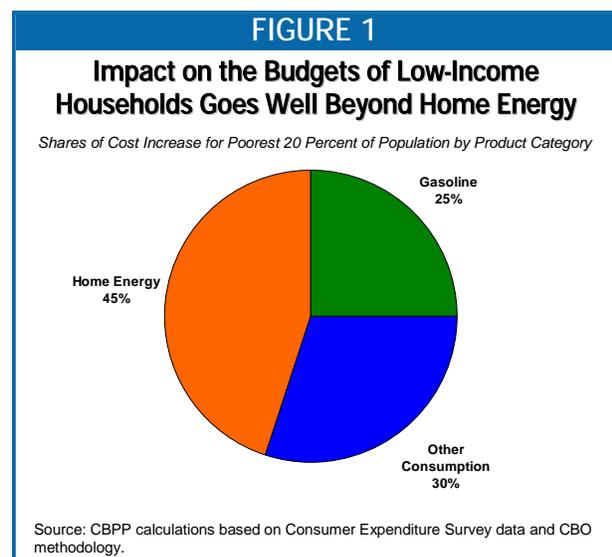
3. A utility company approach is aimed at electric and gas bills, which account for less than half the impact of higher energy prices on family budgets.

The purpose of giving funds to utility companies is to offset increases in electricity and natural gas bills. However, *less than half* of the impact of the legislation on low-income consumers will be felt in the form of higher home energy prices. More than half of the impact will come in higher prices for a range of other goods and services, including gasoline and food (see Figure 1).⁴

Some legislative proposals have sought to address this concern by including a tax cut meant to offset increases in the cost of other goods and services along with funds for utility companies. Depending on how the tax cut is designed, such an approach may help to some degree. However, millions of low-income Americans, including most low-income elderly people and people with disabilities, do not file federal tax returns and likely would not benefit from assistance delivered through the tax code. Problems also would remain for households who do not pay utility bills directly and whose utility costs are reflected in their rents. As a result, this approach would still result in a significant increase in poverty and hardship for millions of lower-income families.

4. Masking the true size of utility bills reduces the incentive to conserve energy.

The goal of low- and moderate-income consumer relief should be to offset the economic hit on those families by restoring their lost purchasing power *without* subsidizing (and thus masking the true costs of) their energy consumption. One of the best ways to encourage energy conservation is for households of all income levels to see the impact of higher energy prices in the bills they pay. Routing assistance through utility companies artificially lowers households' utility bills, and blunts the "sticker shock" of higher bills. People who do not realize that energy costs are going up will be far less likely to take steps to conserve energy or seek out energy efficiency improvements. A rebate, in contrast, protects consumers' purchasing power without blunting the incentives created by higher energy prices.⁵



⁴ CBPP estimate based on data from the Consumer Expenditure Survey and methodology developed by the Congressional Budget Office.

⁵ While consumers receiving a rebate could afford to continue their old energy consumption patterns, there would be a greater payoff to them from doing more conservation and investing in energy efficiency to free up budget resources for other uses.

Requiring utilities to operate programs to help their consumers become more energy efficient would, at best, be a partial solution to this problem. Some utility companies do operate programs that help their consumers with energy efficiency improvements in their homes. Whether to provide significant funds to utility companies for energy efficiency improvements — or to fund efficiency improvements through other mechanisms — should depend upon what is the most effective mechanism to secure such efficiency gains. Even the best-designed energy efficiency programs, however, cannot be relied upon to reach (or fully compensate) tens of millions of lower-income households right away and should not be regarded as a substitute for direct assistance to consumers.

5. It will be extremely difficult to determine an equitable share of federal funding for each utility company.

To provide relief through utility companies, there must be a formula to determine how many of the emissions permits each utility company receives. *But there is no reliable source of information on the percentage of low-income consumers nationally who are served by each individual utility company.* And there are 3,300 of these companies that deliver electricity alone, not counting companies that deliver just natural gas.

Legislative proposals to give funds to utility companies do not distribute them based on the relative incomes of each company's customer base. Some proposals base the distribution on the share of electricity or natural gas that each company delivers. But higher-income communities consume more energy per household, because their homes are larger. So the utility companies in those areas would receive a disproportionately larger share of the resources relative to the needs of their lower-income customers, while utility companies in lower-income communities would be substantially under-compensated relative to their customers' needs. Other proposals base the distribution to utility companies on the emissions they generate — which reflects the amount of electricity they deliver and thus is greater in higher-income areas for the same reason — as well as on the fuel mix used to generate it.

6. Uneven oversight of utility companies will lead to mixed results across the country.

A final obstacle to relying on utilities to deliver consumer relief is the very uneven quality of regulation and enforcement across the states. Most utility customers are served by investor-owned utilities whose rates and practices are regulated by state public utility commissions. Regulators have to work closely with the industry they oversee, and states vary considerably in the degree to which the regulators have successfully avoided being “captured” by the industry. In such a heterogeneous regulatory regime, it would be difficult to provide the federal oversight necessary to make sure that federal funds were used appropriately to protect consumers.

An Alternative Approach: Direct Rebates Coupled With Energy Efficiency Programs

An alternative approach that presents none of these difficulties is to deliver a straightforward “climate rebate” through state debit card systems and the federal tax code. Such an approach also would entail much lower overhead and other administrative costs than trying to use utility

companies as the delivery mechanism. Building on existing public mechanisms would be much simpler and more effective, and less costly, than implementing a new utility-based program.

Why a Utilities-Based Approach Also Is Ill-Suited to Deliver Middle-Class Relief

Many of the reasons that a utility-based approach is ill-suited to provide relief to low- and moderate-income consumers also apply to utility-based approaches for extending relief to middle-income consumers.

- *Inadequate compensation.* Less than half of the impact of higher energy prices on consumers' budgets comes from utility costs. The rest comes from gasoline and indirect costs that arise because energy is used to produce and transport a broad variety of goods and services. Hence, simply providing relief from higher utility costs would leave consumers facing significant cost increases for other items. In addition, tenants whose utility costs are reflected in their rent — and households that heat with fuel oil rather than electricity or natural gas — would not receive relief even for those costs.
- *Lessening incentives to conserve and to invest in energy efficiency.* Consumers who see the true cost of home energy in their utility bills — and who have their purchasing power losses restored through a rebate, rather than through reductions in their utility bills — would be more likely to take measures to lower their utility bills through conservation and investments in energy efficiency than would consumers whose utility bills are artificially reduced by a utility subsidy.
- *Inadequate regulatory oversight.* The heterogeneity among state regulatory regimes raises all the same problems of implementation and oversight in a broader utility-based program as it does in one focused on low- and moderate-income consumers.

These are the most important concerns if utility-based consumer relief for middle-income consumers is paired with appropriately targeted relief for low- and moderate-income consumers through a climate rebate program. If a utility-based approach is the *sole* vehicle for providing relief to consumers, including those with low incomes, the problems increase; under such an approach, low- and moderate-income consumers would be particularly ill-served, for all of the reasons set forth in this analysis.

Here's how a climate rebate would work. Each month, a climate rebate would be delivered to very low-income households through the debit card systems that states already use to provide food stamps and other forms of assistance to low-income families, the elderly, and others. At the same time, low- and moderate-income working families would receive an annual climate rebate when filing for the federal Earned Income Tax Credit (EITC). Through these two mechanisms, rebates could be *automatically* delivered to 75 percent of households in the bottom fifth of the income scale, at very low administrative costs. The remaining 25 percent could sign up for the rebate.

Climate rebates could easily be extended to the middle class as well. (See the box above for problems with using a utility-based approach for middle class relief.) For example, with a little over half of the revenues from a cap-and-trade system, one could provide full climate rebates to households in the bottom 60 percent of the income scale, and partial rebates to the next 20 percent. Married couples making up to about \$110,000 a year (and single filers making up to about \$50,000) would get at least a partial rebate. Under such an approach, debit cards would still be needed to

reach very low-income households who do not file tax returns, but the EITC increase would be replaced with a new refundable climate tax credit.

Importantly, families receiving climate rebates would still face higher prices for energy-related products, and have an incentive to conserve and seek out energy efficiency improvements. Indeed, rebates could be coupled with measures to improve the energy efficiency of lower-income homes and other complementary policies aimed at helping Americans reduce their carbon footprints.