



PolicyPerspective

The “Summer Disconnect”

More Intervention Will Harm, Not Help, Consumers

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Findings

- Proposals for expanded disconnect moratoriums or deferred payment plans shift the focus of these policies from health and safety to income.
- The PUCT does not have the statutory authority to expand deferred payment plans beyond periods of extreme weather emergency.
- An expansion of the moratorium or deferred payment plans will harm Texas consumers—even many of the ones it is designed to help.

Electricity is one of those consumer products or services that have traditionally been the most heavily regulated, subsidized, and/or taxed. Others include telecommunications, insurance, and lending. While government intervention in these areas has often been carried out in the name of protecting consumers, it has in fact more often resulted in harmful, if unintended, consequences.

There has been significant debate in Texas over the last several years whether electricity consumers should always honor their contracts and pay their bills on time, or if there are circumstances where the state should nullify contracts and require retail electric providers (REPs) to offer deferred payment plans for certain consumers.

Specifically, the question is whether poor and/or elderly consumers should be able to get out of their contracts and defer payments of their electricity bills during the hottest summer months—or coldest winter months. This is generically known as the summer disconnect moratorium.

The Public Utility Commission of Texas (PUCT) ordered an emergency moratorium in 2006 on summer disconnections. Similar legislation was filed in the Texas Legislature in 2009, as were related petitions at the PUCT. Neither the Legislature nor the PUCT acted on these, but the PUCT did open a rulemaking process on this issue, and has released at least two draft rules and held several public hearings.

One stated reason driving these proposals has been the health and safety of consumers who may suffer from the extreme temperatures experienced during hot Texas summers. This is a very important concern that, however, is already addressed by current law. The proposals filed in the Legislature and with the PUCT indicate that perhaps the main reason for the summer disconnect moratorium proposals is to alleviate the cost of electric bills for low-income consumers. While the details have varied, the proposals commonly expand the period when consumers can be late on their bills through some kind of deferred payment plan.

This paper will focus its comments largely on the rule changes proposed by the PUCT as published in the Texas Register on April 16, 2010.¹ This paper will also discuss other proposals that have been made for illustrative purposes. In general, the paper finds that the PUCT’s proposed changes on this issue do little to enhance the protection of consumers’ health and safety. Instead, they shift the reason for banning disconnections, i.e., abridging the contractual rights of parties involved, from health and safety to income.

Protections for Public Health in Current Law

Existing Texas law prohibits a REP from disconnecting services of a delinquent consumer when significant health issues are at stake, “No electric utility may disconnect service at a permanent, individually metered dwelling unit of

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a delinquent customer when that customer establishes that disconnection of service will cause some person residing at that residence to become seriously ill or more seriously ill.”²

Additionally, a REP may not disconnect services when the weather is expected to be either too hot or too cold. Specifically, service may not be disconnected in a county when 1) the National Weather Service has issued a heat advisory on a day or on any one of the last two preceding days, or 2) the previous day’s highest temperature did not exceed 32 degrees Fahrenheit, and the temperature is predicted to remain at or below that level for the next 24 hours.³

Additionally, multiple levels of government have provided significant financial assistance to help those without means to pay their bills or to improve the weatherization of their homes—and thus reduce their electricity bills.

The Shift from Health Protection to Income Redistribution

As detailed in the previous section, there is never a situation where a customer who is critically ill—or who would become critically ill—can be disconnected; additionally, consumers are protected from disconnection during the periods of the most extreme weather conditions when health might be most at risk.

These provisions provide significant protection for consumers’ health—in the case of existing health concerns, extreme weather conditions, or both. When adverse impacts on health are known or can be reasonably predicted, consumers will continue to receive service regardless of whether or not they are late in paying their bill.

Whatever the specifics of the different moratorium proposals, they all shift the criteria for eligibility from health and weather to income. In other words, they shift the focus of the state’s disconnect policy from protecting health to assisting low-income consumers.

This paper does not examine the question of whether the state should subsidize the electricity bills of certain consumers. However, should the state continue its current policy of providing this assistance, adopting “summer disconnect”

rules are clearly the least efficient and most harmful way of helping low-income consumers. In particular, they create significant inefficiencies in the retail electricity market, place a heavy debt burden on a few private companies, weaken individual responsibility, and abridge the contractual rights of parties.

Level Billing Options

Current PUCT Substantive Rule 25.480 (h) states that, “A REP shall offer a level or average payment plan to its customers who are not currently delinquent in payment to the REP.” Consequently, every retail electric provider in Texas is already offering some form of an average payment plan to its customers—the best option available for avoiding high summer spikes. Concerns have been raised over the variation in such plans between providers—not every plan operates in an identical manner, so not all customers of all REPs receive the same benefits.

However, this variation is a sign of innovation in the retail electric market. As REPs compete for consumers’ business, they will attempt to create better and more diverse options from which to choose. As consumers choose the REP they feel offers the best options, they can weigh this factor accordingly, along with price, customer service, and all other factors that go into deciding which provider is best for them. If the government steps in and stipulates what each plan should look like, the room for innovation will disappear. Customers will not have the option of seeking the plan that best fits their needs.

In its proposal, the PUCT proposes that REPs “make available, at the customer’s option, ... [t]he opportunity to pay based on a level or average payment plan instead of the balance currently due.”⁴ But this proposal is superfluous. As already noted, REPs must already offer such a plan. But, by putting in the context of the summer disconnect scenario, the proposal encourages consumers to wait until the last possible minute when the bills are highest to get into a plan.

The current level billing options, the system benefit fund that helps pay bills, and the weatherization programs are the least economically harmful ways of helping low-income consumers. They are also the only ways authorized by statute. The next few sections will discuss some other proposed methods that both harm the market and violate current statute.

Deferred Payment Plans

The typical proposal creating deferred payment plans generally calls for a three-month period in the summer or winter in which certain consumers could avoid disconnection by making reduced payments during a defined period. Consumers would be eligible for the moratorium based on their income—usually at or below 125 percent of the federal poverty line. In order to avoid disconnection, eligible consumers could agree to enter into two basic deferred payment plans, one for low-income consumers and the other for low-income elderly consumers.

Although those proposing a deferred payment plan want to help consumers, history shows that many customers will likely fail to repay due to high payments created by the payment plans. Low-income seniors, under some of the plans, could postpone any payments until October by simply agreeing to pay 25 percent of the deferred charges in October and the rest of the remaining balance over the next five months. Below is a theoretical model that shows how deferring costs until October—assuming all payments are made—could significantly *increase* low-income seniors’ monthly bills.

Agreeing to a deferred payment plan is not the same thing as actually making the deferred payments. Conceivably, a customer could avoid paying at all—due to the high initial ramp-up of costs—leaving the company stuck with bad debt and the customer without power. This has too often proved to be the case.

Though its details differ, the deferred payment plan proposed by the PUCT matches previous proposals in seeking to help low-income consumers as well as critical care patients:

(A) The following residential customers are eligible for a deferred payment plan under this paragraph:

- (i) customers receiving, or eligible to receive, the LITE-UP discount pursuant to §25.454 of this title, unless the customer is already enrolled on an average or level payment plan pursuant to subsection (h)(1) of this section;
- (ii) customers designated as critical care and chronic condition customers under §25.497 of this title (relating to Critical Care and Chronic Condition Customers); or
- (iii) customers who have expressed an inability to pay ...⁵

These plans must be offered to any qualified customer who has “a bill that becomes due in July, August, or September” or “in January or February if in the prior month ERCOT records a peak in demand that is higher than the winter peak that existed prior to the winter of 2009-2010.”⁶

However, this proposal clearly conflicts with the Texas Utilities Code, which reads:

(h) A retail electric provider, power generation company, aggregator, or other entity that provides retail electric service may not disconnect service to a residential customer during an extreme weather emergency or on a weekend day. The entity providing service shall defer collection of the full payment of bills that are due during an extreme weather emergency until after the emergency

Low-Income Elderly Option: 25% Payment After Sept. 30th with 5 Month Deferred Payment Plan

	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar
Monthly Bill	\$300	\$300	\$300	\$150	\$150	\$150	\$150	\$150	\$150
Total Balance	\$300	\$600	\$900	\$1,050	\$825	\$690	\$555	\$420	\$285
Deffered Balance	\$300	\$600	\$900	\$675	\$540	\$405	\$270	\$135	\$0
Amount Due	\$0	\$0	\$0	\$375	\$285	\$285	\$285	\$285	\$285
	No Payments			25%	5 Month Deferment Plan				

Source: author’s calculations

is over and shall work with customers to establish a pay schedule for deferred bills.⁷

There are two legal problems with the PUCT’s current proposal.

First, while the statute calls for deferred payment plans to be offered only to those customers whose bills are due during an extreme weather emergency, the PUCT proposal requires they be offered to customers who meet a certain income criteria or profess an inability to pay. Clearly, the legislative intent is to address health and safety concerns, not income.

Second, companies are required to offer the deferred payment plans only during extreme weather emergencies—essentially when the heat index is 105 or above, or the temperature drops to 32 degrees or below. Yet the PUCT proposes that plans be required in June, July, and August no matter what the heat is and during January or February if electrical usage hits a record high. While there is a tenuous connection to weather in the PUCT’s proposal, it is clearly outside the bounds of the statute.

In addition to the legal problems with the current proposal, it will also cause harm to market participants.

A delinquent customer may or may not be able to repay the debt accrued via a mandated deferred payment plan. In either case, an electric company will still have to carry excessive debt for at least three to five months. During the 2006 disconnection moratorium, six retail electric providers (REPs) took on an initial \$16 million worth of customer debt.⁸ Following the moratorium about half of defaulting customers switched to new providers or were disconnected for failure to repay. The average outstanding balance for these delinquent customers was \$785.⁹

Uncollectible debt is a problem that continues to grow. The amount of uncollectible debt created by delinquent customers between January 2008 and July 2009 was over \$229 million.¹⁰ During that time period, 344,624 customers either moved or switched away with a delinquent balance 30 days old or older. In addition, 756,502 of the 1,467,284 customers that were in payment plans or payment arrangements defaulted on their payments.¹¹ In other words, 52 percent of all payment arrangements resulted in default.

Not all electric retail providers are equal in terms of their invested capital. Some companies may be better equipped to deal with a short-term increase in their debt burdens. Others may experience significant financial stress. Encumbering REPs with this kind of debt burden threatens to decrease competition in the electric market by destabilizing smaller retailers. As noted previously, bad debts will ultimately be passed down to the consumer in the form of higher rates or charges.

The Switch-Hold

Electric utilities, coops, and municipal utilities in Texas’ non-competitive areas are legal monopolies. If a customer doesn’t pay his bill, his electricity gets turned off and doesn’t get reconnected until he pays his bill.

That is quite different than the way it works in the general marketplace. A customer who, for instance, uses a J.C. Penney credit card but refuses to pay the bill is free to go shop at Sears. While J.C. Penney can employ various tactics to recover its bad debt, it cannot stop its former customer from making purchases elsewhere.

This is similar to the Texas competitive electricity market today. A REP may go to court to collect past due payments but cannot prohibit a former customer from buying electricity elsewhere.

The reason for this is that the competitive market in Texas has no rule allowing REPs or transmission and distribution companies (TDUs) to impose a “switch-hold” on customers. A switch-hold is when consumers are blocked from switching REPs until they have paid off all past due balances.

A primary reason for the switch-hold as cited by proponents is that it will help to reduce the debt assumed by the REPs who are required by the state to offer deferred payment plans. Additionally, REPs say that a switch-hold lowers their overhead costs by minimizing the need of REPs to resort to debt collection agencies, small claims court, etc. If the debt cannot be recovered from the customer, a REP must recover the cost of that bad debt through its rates to paying customers, or through reduced pay to workers or reduced profits to shareholders. One group of REPS explained the problem that the switch-hold is supposed to address like this:

The bad debt levels experienced by REPs are significant and have substantially grown since the opening of the competitive market. Allowing switch-holds when customers request a deferred, level or average payment plans (which are essentially no-interest loans) is a first step in addressing the bad debt levels.*

This paper is not an examination of debt levels of REPs or why the overall level of debt of REPs has increased since the opening of the competitive market. Neither should it be a concern of the PUCT in its current summer disconnect rulemaking if the level of REP debt has increased because of competition. But the debt created by legally mandated deferred payment plans and level payment plans are a public policy concern that should be addressed. But not with a switch-hold.

The adding of the switch-hold is inconsistent with properly functioning markets; the state first requires REPs to extend risky deferred payment plans which increase their debt, then attempts to deal with this problem with the switch-hold. These interventions are taking the Texas electricity market in the wrong direction.

The Texas market has thrived because—for the most part—the government designed the scope of the market but let the market participants decide how to engage with each other. Requiring REPs to extend credit as proposed, then instituting a switch-hold, harms the market in at least three ways: 1) it increases the cost structure for REPs by requiring the extension of credit in contravention to fundamental credit practices, 2) it introduces substantial administrative inefficiencies in the electricity market, and 3) it will jeopardize the investment of capital into the Texas market, ultimately reducing competition and raising prices.

In an attempt to mitigate some of the harm caused by increased debt, the PUCT has proposed to impose the switch-hold. However, imposing one regulatory intervention to mitigate the bad effects of another never benefits the market or its participants. This is true of the switch-hold as well. The switch-hold will increase system costs, increase inefficiency, and disrupt consumer choice.

The Foundation believes the imposition of the switch-hold and the extension of deferred payment plans will be harmful to Texas electricity markets and top consumers. However, should the PUCT impose the extended payment plans on REPS, it should not do so without also instituting a switch-hold—even though this would harm competition and increase consumer prices. REPs should not be forced to carry debt through actions by the state that abrogate the contractual rights of participants in the electricity market. Additionally, should the PUCT adopt its rules as proposed, and should the switch-hold be invalidated through legislative or judicial action, then the rest of the rule should be invalidated as well.

Early Termination Fees

While not included in the PUCT’s current proposal, previous proposals would have limited early termination fees in various ways, such as banning early termination fees on pre-pay and variable rate products, banning early termination fees during the summer for low-income, disabled, and elderly customers, and pro-rating out of early termination fees. They all amount to the same thing: weakening of individual customer responsibility to the detriment of customers at large. Such a proposal as this would harm, not help, customers. Banning cancellation fees or mandating that they be prorated would void one side of a contract, allowing less and less accountability on behalf of the consumer while requiring the REP to uphold its same level of responsibility. It is quite possible that some REPs would offer precisely these plans. Indeed, it does not appear that any of the variable rate plans have cancellation fees. The voluntary payment plans now being offered by some REPs have already provided a portion of what is being sought by this proposed new regulation. However, by mandating these changes across all REPs, the rulemaking could significantly distort the market, forcing consumers into worse and worse plans as competition is driven from the marketplace. If REPs cannot rely on the income security provided by cancellation fees, they will be forced to hedge their bets against all consumers by raising prices.

Without the proposed regulations on early termination fees, consumers are able to seek out the REP whose services best suit them. Some consumers may highly value the lack of a

* Retail Electric Provider Group, “Initial Comments of the REP Group,” on file at the Public Utility Commission of Texas, #36131 (May 6, 2010).

cancellation fee; others, knowing they are unlikely to change REPs in the near future, value lower prices more greatly. The consumer can make this choice; under the moratorium proposals, the government chooses for all citizens, regardless of their individual needs.

Findings

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- The PUCT does not have the statutory authority to expand deferred payment plans beyond periods of extreme weather emergency.
- An expansion of the moratorium or deferred payment plans will harm Texas consumers—even many of the ones it is designed to help.

Conclusion

Despite existing protections, the calls for a summer moratorium on electric utility disconnections for certain delinquent customers have continued. The PUCT’s proposal would force retail electric providers to take on millions of dollars in bad debts resulting from nonpayment.

Additionally, mandated repayment plans will result in customers who wind up with no electricity and high debt—especially with the proposed switch-hold. Allowing debts—likely larger than individual summer payments would have been—to accrue over the hot days of summer or the cold days of winter will cause many eligible consumers to face even higher debts when the bills finally come due. If they can’t make their payments, then they are likely to lose service.

Who would pay these debts? Not the state, which mandated the payment plans. The burden would fall on the low-income consumers targeted by the moratorium or—in the event of default—on other consumers in the form of higher rates, employees in the form of reduced wages, or shareholders in the form of reduced profits.

Forcing an electric retailer to provide uncompensated services, especially during peak-load months, effectively amounts to a regulatory taking. Regulatory takings are governmental regulations or restrictions imposed on private property to such a degree that the practical effect is a compulsory public taking of value from the property without actually divesting the owner of possession. For all intents and purposes, a rule that forces reallocation or public use of private property—electricity, in this case—without due process or just compensation is a taking of property—whether or not the courts in today’s post-*Kelo* world agree.

In seeking the best outcome for all consumers, the PUCT should not adopt a rule that would require (or forbid) a REP to extend a deferred payment plan to any consumer. This is especially true with the current proposal that shifts the basis for the payment plans from public health to income assistance. To the extent there is a need to help low-income consumers with their electric bills, the appendix lists more effective means of accomplishing this policy goal.

The best approach is to let each REP decide whether to extend a deferred payment plan beyond the current statutory requirements. ★

Appendix: Existing Sources of Funding for Low-Income Energy Assistance

Instead of the proposed moratoriums to help low-income consumers, hundreds of millions of dollars—both in state and federal funds—are currently available for low-income energy assistance. Using existing designated funds is a better alternative to creating a new summer moratorium period.

Federal LIHEAP Funds

The Federal Department of Energy (DOE) and Federal Department of Health and Human Services (HHS) allocated about \$190 million this year to the Texas Department of Housing and Community Affairs (TDHCA) for the Low-Income Energy Assistance Program (LIHEAP). The LIHEAP program consists of the Comprehensive Energy Assistance Program (CEAP)—which targets funds to locally based sub-recipients for the purpose of low-income energy assistance—and the Weatherization Assistance Program (WAP).

TDHCA has already awarded \$123.9 million in funds to 51 of these sub-recipients, including cities, counties, and nonprofit organizations.¹² Through CEAP the department has annually assisted more than 68,000 low-income Texans in all 254 counties. Locally based recipients may accept applications for assistance, determine eligibility, and place priorities on disabled or elderly persons with young children.

CEAP offers a variety of benefits for energy assistance for low-income Texans, including heating and cooling benefits, crisis mitigation, and replacement or repair of unsafe or defective electric equipment. Below is a chart that highlights the eligibility requirements and maximum annual benefit levels. A “crisis” situation may include utility disconnection if the consumer has a good-faith history of bill payments.¹³

CEAP Eligibility Scale and Annual Benefits

Poverty Line	0-50%	51-75%	76-125%
Heating/Cooling	\$1,200	\$1,100	\$1,000
Crisis	\$1,200	\$1,100	\$1,000
Elderly/Disabled	\$1,200	\$1,100	\$1,000
Replacement	\$4,000	\$4,000	\$4,000
Total Max	\$7,600	\$7,300	\$7,000

Source: Texas Administrative Code Title 10, Part 1, Chapter 6, Subchapter A, Rule 6.208

Besides being used for direct low-income energy assistance, 15 percent of federal LIHEAP funds are directed towards weatherization assistance and outreach. Special attention is paid to elderly or disabled individuals or households with significant energy burdens.¹⁴ Households that meet the income requirements are also eligible for up to \$4,000 in equipment repair or upgrades for unsafe or inefficient appliances. Appliance upgrades or replacement may help alleviate future month-to-month costs for low-income households.

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System Benefit Fund

In addition to federal funds allocated from the HHS and the DOE through LIHEAP, money for low-income energy assistance is held in the System Benefit Fund (SBF) and implemented through the LITE-UP Texas program. The SBF is an account held within the general revenue fund that can be appropriated only to assist low-income electric consumers in deregulated markets. Retail electric customers in these markets pay 65 cents per megawatt hour on their monthly utility bill to fund various low-income energy assistance programs including 1) rate reduction, 2) bill payment assistance for ill or disabled persons threatened with disconnection, 3) consumer electric choice education, 4) energy efficiency assistance programs, and 5) administrative reimbursements.¹⁵ If this rulemaking is passed, these customers will find themselves not only paying to fund other people's utility bills directly, but also watching their own rates rise as REPs are forced to cover the costs of this new government mandate.

The SBF currently has an estimated account balance of almost \$930 million available for appropriation in the 2010-11 biennium. Just \$240 million from this fund has been allocated, leaving a surplus of more than \$680 million.¹⁶ In order to alleviate the dangers and discomforts due to summer electric disconnection, the Legislature could have appropriated some of the surplus SBF funds for additional low-income or crisis assistance. Currently, an eligible consumer lives at 125 percent or below the federal poverty line; receives food stamps from the Texas Department of Human Services; or participates in a medical assistance program administered by the State. As the Legislature chose not to allocate this spending further, it is inappropriate for an agency to force electric consumers to further bear this burden in the Legislature's stead. ★

Endnotes

¹ Public Utility Commission of Texas, Project 36131, "Proposal for Publication Of Amendments To §§25.454, 25.480, and 25.483 as Approved at The April 1, 2010 Open Meeting" (5 Apr. 2010).

² Texas Administrative Code, Title 16, Part 12, § 25.29(g).

³ Texas Utility Code, Sec. 39.101 (h), and Texas Administrative Code, Title 16, Part 12, § 25.29(g).

⁴ PUCT, "Proposal for Publication," 11.

⁵ *Ibid.*, 10.

⁶ *Ibid.*

⁷ Texas Utility Code, Sec. 39.101(h).

⁸ Aggregated Study by Direct Energy, "Critical Care and Low Income Customers Served by Retail Electric Providers" (20 Apr. 2009); PUCT Project 34400.

⁹ *Ibid.*

¹⁰ Aggregated data from REPs representing 25% of market, Jan. 1 2008 to July 31, 2009.

¹¹ *Ibid.*

¹² Press Release, "State rushing \$123.9 million in funds to help low income Texans offset high utility bills," Texas Department of Housing and Community Affairs (22 Jan. 2009).

¹³ Texas Department of Housing and Community Affairs 2009 LIHEAP Application.

¹⁴ TDCHA 2009 LIHEAP Application.

¹⁵ Texas Utilities Code Chapter 39 Section 903.

¹⁶ HCSSB 1, Texas 81st (R) Legislative Session, http://www.lbb.state.tx.us/Bill_81/4_House_Full/Bill-81-4_House_Full_0409.pdf.

