

RECOMMENDED INDIANA UTILITY REPONSES TO CREDIT AND COLLECTION OUTCOMES IDENTIFIED IN 2006 ANNUAL COLLECTIONS REPORT

By:

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This memo sets forth a set of recommendations for the State of Indiana's improvement in credit and collections outcomes. The recommendations are based on the data presented in the 2006 annual report on credit and collections presented to the Coalition to Keep Indiana Warm in October 2006. That annual report presents information on credit and collections for the reporting period July 2005 through June 2006. The data includes information both on low-income customers—customers are defined to be “low-income” if they are recorded as having received fuel assistance through the federal Low-Income Home Energy Assistance Program (LIHEAP) in the current year—and for residential customers as a whole. Low-income customers are a subset of the total residential customer population. The data does *not* present low-income customers and non-low-income customers. The discussion below will set forth the recommendations and reference the particular data in the annual report giving rise to the recommendation.

#1. Energy Efficiency as an arrearage management technique.

Indiana utilities should use energy efficiency investments as an arrearage management technique. The data in the 2006 Annual Report supports the conclusion that accounts in arrears have higher average usage than accounts not in arrears.¹

The conclusion that bills for accounts in arrears are higher than not is true for both residential accounts generally and for low-income accounts in particular. While the Annual Report does not directly report consumption data for accounts in arrears, the conclusion can nonetheless be derived from the data in the Annual Report. For residential accounts as a whole, while 21% of all *accounts* were in arrears in an average month during the 2006 reporting period,² 28% of all *revenue* was in arrears (on

¹ This is not to say that all high usage accounts are in arrears. It merely suggests that accounts in arrears tend to have higher than average usage.

² The 2006 reporting period covered July 2005 through June 2006.

average). (Table 3).³ Since the proportion of revenue in arrears is *higher* than the proportion of accounts in arrears, each account in arrears must have a higher than average amount of revenue.⁴ If accounts in arrears had average consumption, in other words, the proportion of accounts in arrears and revenue in arrears would be the same.

The phenomenon of arrears being associated with higher than average bills is even greater for low-income customers. While, on average, 31% of all low-income accounts were in arrears in any given month in the 2006 reporting period, 54% of low-income revenue was in arrears. Since the difference is greater, the disproportionate contribution of each low-income account in arrears must be greater as well.⁵ The fact that the difference in proportions is so much higher for low-income customers than for residential customers provides evidence of the inability of low-income customers to absorb higher than average bills. As bills for all customers increase above average, these customers are more capable of absorbing the extra costs. In contrast, low-income customers do not have the capacity to absorb those higher-than-average bills.

Different energy efficiency strategies could be targeted to accounts in arrears. For accounts substantially in arrears in a persistent fashion, comprehensive weatherization treatments (or prioritization for comprehensive treatments) may be in order. For accounts with lower usage, and fewer or less persistent arrears, mass distribution of low-cost efficiency treatments⁶ may be more justified. The lower costs allows a broader distribution of such kits which, while not generating substantial energy/water savings, may generate sufficient savings to help address the lower and less persistent arrears.

#2. Increase penetration of Budget Billing.

Indiana utilities should increase the penetration of Budget Billing as an arrearage prevention technique.⁷ Levelized Budget Billing plans help customers avoid the “peak” in utility bills that often accompanies winter heating load. Increasing the use of Budget Billing could occur in three ways:

- First, utilities could remove barriers to participation in Budget Billing programs. A common barrier, for example, is the requirement that a customer not be in arrears at the time he or she enters the Budget Billing program. Indeed, Budget Billing may be most beneficial to those customers that *are* in arrears. It is the fact of arrearages that evidences the need to address the high winter bills with which to begin.

³ References are to tables in the 2006 Annual Report.

⁴ Since accounts in arrears are higher than average, the accounts *not* in arrears must be lower than average. The difference between accounts in arrears and those not in arrears is thus even greater than the difference between accounts in arrears and all accounts on average.

⁵ There is no information on individual accounts. Data is collected in the aggregate.

⁶ A Portland (OR) firm distributes a popular low-cost energy and water efficiency kit that can be used on a mass basis. The firm, quantec, llc, has used these kits around the nation.

⁷ For these purposes, “budget billing” involves a process through which an estimated annual bill is billed in equal monthly installments over a 12-month period.

- Second, utilities could use Budget Billing to incentivize payment behavior. Many utilities, for example, do not allow customers to enter Budget Billing during the winter months. An alternative decision-rule might be that a customer could enter a Budget Billing program during cold weather months if the account is current immediately before the first cold weather month (or if certain minimum payments have been made) (e.g., if you paid 75% of your winter bills to date, you will be allowed to levelize the remainder of your winter bills over a longer period of time).
- Third, utilities could incentivize the use of Budget Billing. For example, the offer of a 10-month Budget Billing plan, allowing a customer to “skip” making payments in two months of the customer’s choice, might be attractive to customers who do not wish to make utility payments in months with high amounts of competing expenses (e.g., holiday expenses, back-to-school expenses).

Indiana utilities have a very low penetration of Budget Billing, both for low-income accounts and for residential accounts in general. On average, 20% of residential accounts are on Budget Billing. (Table 6). That percentage does not vary significantly by month or season. In contrast, on average, only 11% of low-income accounts are on Budget Bills. There appears to be more monthly and season variation⁸ for low-income accounts (varying between 9% and 15%) compared to the total residential variation (between 19% and 20%).

Two issues thus present themselves by the Indiana Budget Billing data. First, how is it possible to increase the overall penetration of Budget Billing? Second, why is the penetration of Budget Billing in the low-income population so much lower than in the residential population generally, and how can the barriers specific to low-income customers be addressed?

#3. Seasonal Budget Billing as an arrearage management technique.

In addition to incentivizing (as well as removing barriers to) participation in Budget Billing, Indiana utilities might wish to consider offering an alternative Budget Billing option. Experience counsels that many customers do not wish to enter into Budget Billing that significantly increases their warm weather month bills. Even though the whole purpose of Budget Billing is to time-shift part of a bill, the realization that the elimination of the high winter bill also means the corresponding elimination of the low summer bill (assuming a natural gas customer, that is) creates a barrier to Budget Billing enrollment.

⁸ One question that should be watched in future annual reports is whether the 15% penetration in July is a seasonal uptick in Budget Bills or whether it was an aberration in the 2006 data.

Given this recognition, Indiana utilities might be well-served to offer something other than an annual Budget Billing plan. A “summer free” plan would help guard against the high winter bills while also preserving the low-cost summer months for the customer. The data clearly shows that many customers in arrears are simply engaging in short-term time-shifting of high winter bills without the structure of a Budget Billing plan. Increases in monthly arrears for the residential class as a whole truly begin with the January bill. Moreover, by May, those arrears are being significantly paid down. (Table 2). The same is true for low-income customers, with both the number of accounts in arrears and the average monthly dollars in arrears showing a sharp increase in January, with dramatic and prompt “pay down” in the months immediately following the winter. (Table 11). To allow customers to move some of that time-shifting forward rather than having it merely be backward would be consistent with the desire to keep bills paid, and the demonstrated inability to make that happen in the high cost winter months. To move some of those January through March dollars forward to the lower cost months immediately preceding winter should help lower arrears without running afoul of the customers’ desires to retain their low-cost summer bills.

The benefits of Budget Billing can be demonstrated by more than reference to actual monthly bills (and the seasonable variation in those bills). The benefits can be ascertained by reference to the “bills behind” statistic as well. Within the residential population as a whole, those accounts in arrears maintain a reasonably consistent number of “bills behind” over the entire year. So, while the dollars of arrears certainly increase during the winter months (Table 2), the number of payments missed varies in a reasonably narrow band around about 1.25 “bills behind.” There is a slight uptick in January (to 1.33).⁹

What the data shows is that roughly the same number of bills are unpaid in any given month throughout the year. Higher dollar levels of arrears occur in the winter months, however, simply because each unpaid bill in the winter month is worth more dollars. As can be seen, therefore, if some portion of those winter bills could be moved forward to a month with a lower “bills behind” statistic, even if the “bills behind” statistic could not be lowered, the overall revenue in arrears would be less since each “bill behind” would relate to a smaller bill.

The same phenomenon is true for low-income accounts. There is a moderate increase in the number of “bills behind” during the winter months (from 1.41 in January to 1.79 in March).¹⁰ As with residential accounts, even if Budget Billing could not reduce the number of “bills behind,” each bill would be smaller and the total revenue in arrears should decrease. In fact, it would be reasonable to expect that Budget Billing would reduce the total number of “bills behind” as well. Accordingly, two favorable results

⁹ It is not clear why there is a July increase in the number of “bills behind.” It could be that some customers that are disconnected for nonpayment of winter bills continue without service, but do not retire those winter arrears. As a result, when the winter arrears are compared to summer monthly bills, the result is a high “bills behind.” The actual cause for the dramatic increase in bills behind during July, however, has not yet been determined.

¹⁰ Note that the “bills behind” statistic for low-income accounts noticeably declines in November (down to 1.30). The likely cause of this decline is the receipt of LIHEAP payments that allow overall low-income arrears to temporarily diminish.

would arise: (1) fewer bills would be outstanding; and (2) each outstanding bill would be smaller, with total revenue in arrears declining as a result.

#4. Understanding “no reconnect” accounts.

Indiana utilities should develop a better understanding of their *disconnected* accounts that do not *reconnect* to the system. There is a substantial population of accounts that do not appear to reconnect to the utility system after service has been disconnected for nonpayment. Within the residential population as a whole, Indiana utilities reconnect, on average, 62 accounts for every 100 accounts that are disconnected for nonpayment. (Table 8). Perhaps surprisingly, the proportion of *low-income* accounts that are reconnected after a disconnection for nonpayment is higher, with a monthly average of 77 low-income reconnects for every 100 disconnects for nonpayment. (Table 17).

Over the course of a year, the absolute magnitude of the difference between disconnects and reconnects can be substantial. For the total residential class, while 18,375 accounts were disconnected each month (Table 7), only 11,371 were reconnected. (Table 8). For low-income customers, while 1,763 accounts were disconnected on average each month, only 1,354 were reconnected. (Table 17). Over the course of the year, there were nearly 5,000 more low-income disconnections than there were low-income reconNECTIONS.

Indiana utilities should inquire into what happens when an account is not reconnected. Is the account reconnected in a different name? Does the customer go without utility service? Does the disconnected customer change residences and be replaced with another customer at the disconnected service address? Is the home completely abandoned? A utility need not track the specific customer in order to determine what happens at the service address.

Finally, Indiana should emulate Pennsylvania is requiring utilities to engage in a pre-winter termination survey. This survey involves checking each service address that has had service disconnected but not reconnected since the beginning of the last winter heating season¹¹ to determine whether someone is living at that service address, whether that resident is taking service unlawfully, whether the resident remains without utility service entering the winter heating season, or whether the housing unit has been abandoned. This winter survey occurs immediately before the start of each winter heating season.

¹¹ One need not consider whether service was reconnected to the same customer, for purposes of the winter survey, but only what happens with the service at a particular address where service had been terminated for nonpayment.

#5. Targeted EITC outreach as an arrears management technique.

Indiana utilities should engage in outreach for the federal Earned Income Tax Credit (EITC) targeted specifically to winter month payment-troubled customers. Little question exists but that high winter bills pose an affordability problem for low-income Indiana utility customers. While 22,513 low-income accounts were in arrears in September 2005, with an average past-due balance of \$101, 64,612 low-income accounts were in arrears in March 2006, with an average past-due balance of \$285. By May 2006, the average past-due balance had decreased to \$172, while the aggregate dollars in arrears had decreased from a peak of \$18.4 million (March) to \$10.5 million (Table 11). During the winter months, the low-income accounts in arrears experienced an increased nonpayment of nearly one-half month (from 1.41 bills-behind to 1.79 bills-behind) before decreasing to more normal levels by May. (Table 11).

Targeting EITC outreach to payment-troubled customers meeting a minimum level of arrears would help address this problem. If a “trigger” amount for such outreach is appropriately set, it is likely that the account in arrears would be low-income. While there is a significant increase in average past-due balances for the total residential customer base (from \$101 in September to \$202 in January) (Table 2), it does not approach the increase in low-income arrears (from \$101 in September to \$285 in March). (Table 11). And, as mentioned previously, the average total residential bills-behind remains relatively constant in cold weather months (Table 2), while the low-income bills-behind statistic does not (Table 11). If EITC outreach is targeted to accounts with an average arrears noticeably higher than the total residential average (e.g., \$300), it is more likely than not that the account will be low-income.

Engaging in EITC outreach targeted to customers in arrears is likely to have a positive impact for both the customers and the company. The average EITC benefit nationwide is \$2,000. More than one-third of all households that receive an EITC benefit use that benefit to pay a past-due utility bill. The proportion of those households that are in arrears which use the EITC to help pay their bills is thus likely to be much higher. To the extent that customers are substantially in arrears during the months of January and/or February, assisting them to claim any EITC benefits to which they are entitled would be a financial benefit.

#6. Incentivize/decrease barriers to deferred payment arrangements.

Indiana utilities should focus increased attention on enrolling customers with arrears in deferred payment arrangements. A fraction of residential customers in arrears in 2006 enrolled in a deferred payment arrangement as a mechanism to help retire those arrears. On average, in 2006, only five percent (5%) of Indiana residential accounts in arrears were subject to payment plans. (Table 4). Not all arrears should be subject to payment plans, of course. Accounts that have either small (or short-term) arrears do not necessarily merit deferred payments. Indeed, the fact that the average percentage of revenue in arrears subject to payment plans (13%) each month (Table 5) is nearly

triple the average percentage of accounts in arrears on payment plans indicates that the average arrears subject to payment plans is substantially higher than the average arrears overall.

The average monthly proportion of low-income arrears subject to payment plans is noticeably higher than the average proportion of residential arrears generally. On a monthly basis, 12% of all low-income accounts in arrears were subject to agreement, with the percentage rising in the months immediately subsequent to the winter heating months (19% in March, 17% in May). (Table 13).

There is a substantive difference between low-income arrears and the arrears of residential customers generally. In contrast to the total residential population, however, as a general rule the proportion of low-income revenue subject to agreement was lower than the proportion of low-income accounts subject to agreement. Only in one month (May 2006), which appears to be a one-month aberration, did the percentage of low-income revenue in arrears subject to agreement exceed the percentage of low-income accounts in arrears subject to agreement. (Table 14). The significance of this data is that the low-income accounts with higher levels of arrears are not entering into deferred payment arrangements, let alone successfully completing them.

At a minimum, additional inquiry should be made into why low-income customers in substantial arrears are not entering into deferred payment arrangements. The reason for this phenomenon might be that barriers exist that affirmatively impede such payment plans. Such barriers might include downpayment requirements that are too high or payment plan terms that are too short (making monthly payments impossible to meet). The reason might involve a utility company refusal to enter into second payment plans if a first payment plan results in a default. The reason might be that low-income customers with substantial arrears recognize that their bill for current service is unaffordable and that, accordingly, any agreement to pay the bill for current service while at the same time seeking to retire arrears would be a fruitless endeavor. The reason might be that the higher arrearage amounts for low-income customers are more likely to have resulted in a shutoff and that, accordingly, payment plan pre-requisites involve the payment of reconnect fees and/or deposits that serve as barriers to entering into a deferred payment plan for the underlying arrears.

The remedy for the failure to enroll low-income customers in arrears in deferred payment plan agreements depends, of course, on the underlying cause for the failure. Smaller downpayments and longer terms may well be merited. One remedy, also, might address those arrears that have escalated beyond a range that might involve any reasonable opportunity to retire. In those instances, Indiana utilities might wish to consider entering into payment plans for less than the entire outstanding arrears. If a low-income customer owes \$2,000, in other words, the utility might reasonably enter into a payment plan for \$600. Such an approach recognizes that an incremental approach might lead to more positive long-term outcomes than an “insistence” that the

arrears be subject to an agreement that either disincentivizes the customer from entering into such an agreement or an agreement that is destined to fail.¹²

A utility might create incentives for a low-income customer to enter into a deferred payment plan for some portion of a large and unretirable arrears. For example, an agreement to waive late payment fees on the portion of the arrears not subject to the payment plan so long as the payment plan is current might be an effective incentive. On an arrears that is large enough to qualify for such a split payment plan, waiving such fees could deliver real dollars of benefit to the customer.

#7. Sharpen the criteria for issuing notices of disconnection for nonpayment.

Indiana utilities would be well-served to sharpen the criteria they use for issuing notices of disconnection of service for nonpayment. The state's utilities appear to send far more notices warning of the disconnection of service for nonpayment than they are either willing or able to actually implement. Unfortunately, when a utility consistently threatens the disconnection of service if payment of an outstanding bill is not made by a date certain, with no follow-through on that warning, customers eventually learn that the notices of disconnection are a false threat that can be safely ignored without consequence.¹³

Indiana utilities issue a high percentage of "false" warnings of an impending disconnection for nonpayment each month. Within the residential population as a whole, Indiana utilities tend to issue between 15 and 20 disconnect notices for each disconnection of service actually performed. Indiana utilities have a notice-to-disconnection ratio of 15.8 on an average monthly basis, with the specific monthly ratios ranging from a low of 12.9 in May to a high of 19.0 in November. Perhaps more significant than the ratio, however, is the absolute magnitude of the number of disconnect notices that do not give rise to the actual disconnection of service. Even in the month with the "lowest" ratio (12.9-to-1 in May 2006), Indiana's utilities issued nearly 365,000 disconnect notices, while disconnecting "only" 28,344 accounts for nonpayment. In May, in other words, Indiana utilities issued more than 336,000 notices warning of termination for nonpayment that never occurred.¹⁴ Over the twelve-month reporting period, Indiana utilities issued 3.5 million disconnect notices while terminating service to only 0.2 million accounts for nonpayment. (Table 7).

¹² In this regard, one can be mindful of the baseball team that is down three-games-to-none in a seven game League Championship Series. The team is well-served by the attitude that they do not need to "win four games" to win the series. They need only win "tomorrow." Taking it "one game at a time" may be a cliché, but it is accurate nonetheless. That first \$600 in arrears is the equivalent to Game Four in that seven game series.

¹³ This discussion sets aside the question of whether issuing notices warning that service disconnection will occur in the absence of payment, when such disconnection is not likely to happen, presents a legal issue. See e.g., *Palmer v. Columbia Gas of Ohio*, 479 F.2d 153 (6th Cir. 1973).

¹⁴ Some of these disconnections, of course, were presumably avoided by customers paying their bill.

On average, the issue with low-income customers is about the same. In the 2006 reporting period, Indiana utilities issued 15.2 notices warning of a service disconnection for nonpayment for every disconnect that they actually performed. Over the course of the twelve-month reporting period, Indiana’s utilities issued 321,000 disconnect notices to low-income accounts while performing 21,000 disconnections.

The problem with issuing disconnect notices that do not lead to the disconnection of service is that the notices eventually destroy the efficacy of their “message” that “consequences will flow if you do not make a payment.” Indeed, in many ways, “over-noticing” customers may well lead to an *increase* in the number of ultimate service disconnections. Since some resource-constrained customers will leave payment until the last possible moment, as measured by the imminent disconnection of service, a series of shutoff notices that do *not* lead to such disconnections may lead to customers to ignore notices that they should not. There is no way for a customer to tell the difference between a notice issued when the utility “really *means* it, this time” from one that is not issued under such circumstances.

The problem was addressed by the courts in an Ohio case involving Columbia Gas. In referring to a “flood of final notices” that was not followed up by an actual service disconnection for nonpayment, an Ohio federal judge referred to the company’s practice of “a wolf kind of notice which does not conform to the constitutional requirements that notice be truly informative and be given at a meaningful time.” The judge explained:

Several thousand years ago, I believe there was a writer who told the story about a boy who thought he would cause excitement by crying that the wolf was attacking his flock of sheep. It did cause excitement, but since no wolf was attacking, after he had stirred up excitement a couple of times, when the wolf really did attack nobody paid any attention to him. So that what we have here is a wolf kind of notice that is very convenient for the computer to issue, but is not, I think, what the statute [O.R.C. § 4933.12] contemplates, which, in my interpretation, is a meaningful notice that applies to the person who is going to be affected by it and will be followed by some action.¹⁵

Quite aside from the legal implications, the over-issuance of disconnect notices impedes the collection efficacy of these notices. Indiana’s utilities should investigate their ability to better define the circumstances under which a service disconnection is likely to occur and restrict the issuance of disconnect notices to customers falling within those circumstances.

Conclusion and Summary

The Annual Report generated by the Coalition to Keep Indiana Warm can be used for far more than documenting the credit and collection outcomes for Indiana utilities each year. The data can (and should) also be used to identify areas where initiatives, large

¹⁵ 479 F.2d at 166 – 167.

and small, could generate specific measurable improvements in those collection outcomes. The initiatives may, but need not, be directed to low-income customers in particular. While some initiatives might be directed to residential customers generally, they might nonetheless still have a disproportionately positive impact on low-income customers.

The following recommendations are supported by the 2006 Annual Report:

- Pursuing energy efficiency as an arrearage management technique;
- Pursuing efforts to increase penetration of Budget Billing;
- Offering seasonal Budget Billing as an arrearage management technique;
- Undertaking survey research to generate understanding of the “no reconnect” accounts;
- Targeting EITC outreach as an arrears management technique;
- Adopting measures both to create incentivize and to remove barriers to deferred payment arrangements; and
- Sharpening the criteria for issuing notices of disconnection for nonpayment.