

Economic Opportunity Studies

On-Bill Repayment for Home Energy Efficiency: *The Benefits and the Risks*

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EFFICIENCY:
*THE BENEFITS AND THE RISKS***

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Abstract

Loans that pay for residential energy efficiency upgrades and are repaid with monthly utility bills are a potential source of low-cost, easy-access capital for building owners. In the past 5 years, many utilities and a number of states have enacted laws or regulations governing these on-bill repayment initiatives and have implemented programs in the residential market.

The risks to borrowers and utilities have not been examined to same degree as have the potential benefits. For most of the emerging programs, the consumer protections that are required elements of conventional consumer loans from regulated lenders are not explicitly included; among such policies would be disclosure of penalties, grievance procedures and adjudication regarding either services purchased or loan servicing. Nor are there standards for disclosures regarding borrower obligations upon transfer of occupancy. Borrowers who are tenants face more uncertainties. Additional risks face consumers with very low incomes, including potential reduction of bill payment assistance benefits without a similar reduction in the billed amount and a greater likelihood of extended periods of disconnection.

This paper focuses on risks that must be considered by regulators, legislators and financing partners. It develops an agenda of questions and analyses that advocates for residential customers in general and for low-income populations in particular should ensure are addressed in program design and implementation.

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On-Bill Repayment for Home Energy Efficiency: *The Benefits & the Risks*

Executive Summary

On-bill repayment for loans that pay for residential energy efficiency upgrades are a potential source of low-cost, easy-access capital for building owners. In the past 5 years, many utilities and a number of states have adopted laws or regulations governing these initiatives and have implemented them in the residential market. The risks to borrowers and utilities have not been examined to same degree as have the potential benefits. This paper focuses on risks that must be considered by regulators, legislators and financing partners and presents an agenda of questions and analyses specific to each risk. Advocates for residential customers in general and for low-income populations in particular are offered a list of issues to address regarding OBR program design and implementation is provided for.

Very few on-bill initiatives carry consumer protections that are as protective as those required for a conventional consumer loan from regulated lenders. Among the differences: most do not address the disclosures about loan terms, penalties and warranties nor contain procedures for correcting errors on an account; most do not protect a consumer's credit rating during dispute proceedings nor define privacy rights of the borrower; most also lack clear disclosure guidelines regarding how post-upgrade payments and bills will compare with prior utility bills. A number do not resolve the question of responsibility for payments by borrowers who move. However, nearly all allow disconnection of utility service in the event of non-payment of the loan portion of the monthly bill. This penalty compares unfavorably to allowable debt collection practices for other types of consumer loan.

There are additional serious risks to low-income borrowers; first, the affordability of a bill that remains at past levels during the repayment period [i.e. achieves "bill neutrality"] is in question for those whose current bills are un-affordable. Further, participation may mean reduced assistance from federal, state and utility bill assistance programs because the loan is ineligible for support. Low-income customers move with dramatic frequency as compared to higher income groups, and are more likely to be tenants. These and other concerns studied suggest this is one market segment that should not be targeted for this new form of lending.

Introduction to On-Bill Consumer Financing

Over the past two decades, multiple small-scale on-bill-financing (“OBF”) or on-bill-repayment (“OBR”) programs were created as a means to easily finance and encourage energy efficient upgrades.¹ While most of the resources in the past were directed to commercial-scale buildings and equipment, a recent development is the extension of such financing options to households. Now, many states are considering implementing full-scale residential on-bill financing and repayment programs. As of late 2012, utilities in more than a dozen states have on-bill financing and repayment options. A minority of these have existed long enough to demonstrate their results.² Utility companies market these programs as a no-cash-down, easy-access way to pay for durable investments in cost-effective efficiency upgrades.

OBF programs are not identical to OBR programs, but both offer energy consumers a way to invest in energy efficient upgrades to their home or commercial property by using a loan that is easily obtained and has favorable terms. Customers pay back that loan as part of their utility bill payment. Most programs offer these as unsecured loans at below-market interest rates without regard to customers’ credit history.³

Lenders that finance the initiatives view these loans as low-risk because consumers are more likely to pay their utility bills than other unsecured loans.⁴ Recently, federal and state subsidies that further enhance the attractiveness of the offers have been available. Some utilities and policymakers believe these loans are a tool well-suited to low-income consumers seeking to lower energy bills. This group lacks access to commercial credit and has limited savings to use for energy upgrades than do others. Energy Secretary Chu has suggested introducing loans as the primary financing tool for upgrading low-income housing, replacing much of the federal Weatherization Assistance Program.⁵

This paper describes current and emerging residential on-bill programs, their results thus far, and important unresolved policy and legal questions. It includes consideration of the unique characteristics of the Weatherization Assistance-eligible population that could affect the energy and economic results of relying on a lending strategy to include lower-income consumers in the retrofit strategies of states.

Defining On-Bill Programs

The difference between on-bill financing [OBF] and on-bill repayment [OBR] programs is determined by the source of the capital for the loans. OBF means utility shareholder or ratepayer funds are loaned by the utility.⁶ Borrowers in OBF programs may not be protected by federal consumer lending laws, because the owner of the funds may not fall within the category of lender⁷ whose actions are regulated by federal law. OBR programs use third-party capital.⁸ Much of the current financing has come from state bonds or private financing organized for the purpose. To date, many private third party investors are specialized lenders, some incorporated solely to offer utilities financing. Other experienced mortgage lenders offer loan pools for residential retrofits. Recently, larger entities such as Citibank have been getting involved.⁹

In some states where these programs' collection practices are limited by a statute which prohibits utility companies from disconnecting a consumer's power for non-payment of a third-party loan many private third-party lenders are wary of entering into the market where they must offer a low interest rate without the sanction to guarantee a low-risk of default.¹⁰

The Accelerating Trend to Offer OBR Options

Financing programs have a longer history than on-bill repayment programs, because they are generally easier to implement. A third-party lender does not have to be involved and in many states legislation is unnecessary.¹¹ Capital may come from ratepayer or corporate funds.¹² However, on-bill financing is also constrained by the same attribute that makes it relatively simple to implement: utility funds are limited and loan servicing is not a utility expertise.¹³

Despite a twenty-year longer history than OBR programs, OBF is viewed as not as effective in reaching the scale of today's energy efficiency goals.¹⁴ In an OBF program the utility company takes on the role of a financial institution, and may be subject to financial regulations applicable to bank lenders, such as being required to abide by the federal Truth in Lending Act, the Equal Credit Opportunity Act, and the Fair Debt Collection Practices Act. Courts have not determined whether a utility company lending out ratepayer funds is considered a "creditor" as defined by these federal consumer protections.¹⁵

OBR programs, where a third-party provides the funding and typically takes on much of the loan servicing and related administrative work, may shift the regulatory responsibilities to the source of the capital. These have been a much more recent development.¹⁶

While legislation requiring these types of programs is still in its infancy throughout the country, twenty states have utilities with either on-bill residential retrofit financing or on-bill residential repayment program options; eight¹⁷ of the twenty states enacted recent legislation supporting or changing on-bill repayment programs since 2007.¹⁸ Michigan paved the way with a statute that became effective in October 2008 and allowed residential on-bill loans to attach to the meter as opposed to the borrower.¹⁹

In California, 2009 legislation directed the state Public Utilities Commission to open a proceeding “to investigate the ability of electrical corporations and gas corporations to provide energy efficiency financing options to their customers;” “financing options” include “on-bill financing.”²⁰ Pursuant to the statute, the CPUC opened a proceeding and released a proposed decision on March 20, 2012 stating its intention to establish a two-year transition period for putting into place new energy efficiency financing programs.²¹ Over the next two years, utility companies are expected to devise OBF program designs with offerings of at least \$200 million per utility for loans to commercial customers, including some multi-family buildings but not small residential properties.²²

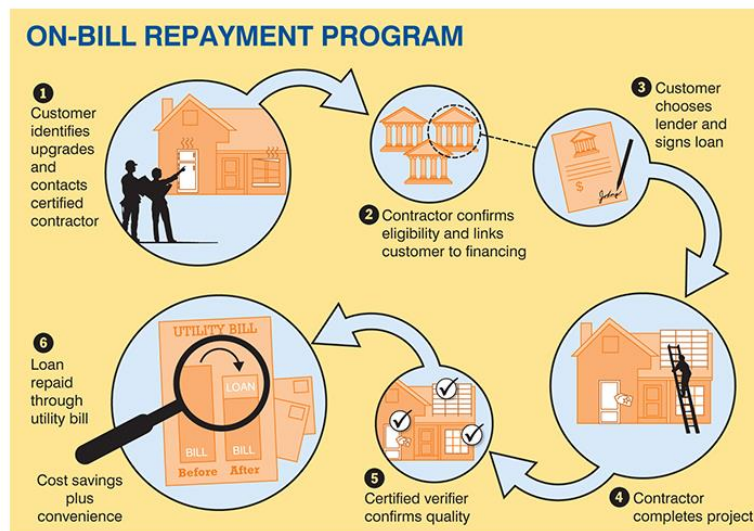
Following 2011 legislation in New York, the state’s energy authority, NYSEDA, began implementing an on-bill “recovery” program. New York’s program is unique in that the state’s longstanding Home Energy Fair Practices Act protections attach to on-bill recovery or financing. They include a prohibition on utility disconnection for payment issues between November 1 and April 15 and significant safeguards for the elderly and disabled.²³

One significant, but modest, federal initiative was launched when the Rural Utilities Service [RUS] proposed a rule initiating an Energy Efficiency and Conservation Loan Program in July 2012. It would make available \$250 million for on-bill financing.²⁴ In the past, the RUS would defer the repayment of electric cooperatives’ loans to give the companies more freedom to offer these programs with their own capital.²⁵

How OBR Works

Although programs differ, the typical engagement between utility and customer starts when a consumer approaches his or her utility company either looking for ways to lower energy bills or seeking help in installing energy efficient upgrades; many are responding to outreach for the program. A contractor selected from a utility-approved list will assess the home and make a bid to perform the improvements. Many utilities subsidize the assessment. The contractor in many programs is the party that explains the loan terms to the owner, although in some states the lender and owner execute the arrangements directly. Typically, the contractor assists the homeowner in filling out the loan application and application for any rebates available; most such programs do not conduct an independent credit check, although many treat poor utility bill payment history as disqualifying.

If selected by the owner, the contractor will perform the services and submit the invoice to the utility. The utility company will have a representative check the work, and will then pay the contractor for the services. Loan payments and servicing fees will then appear on the consumer's bill.²⁶



Source: Environmental Defense Fund

Benefits of On-Bill Repayment Programs

OBR residential programs offer potential benefits to household consumers, building owners and the environment as well as to the growing sector of efficiency lenders. These programs make energy efficient upgrades available to a wider range of customers; their favorable terms and ease of access are

sufficiently attractive to get the attention of marginally-interested households. Consumers, typically building owners but sometimes a renter, appreciate the ease of access and the potential for lower energy bills in the future. The effect of greater retrofit investment meets carbon-reduction and other regulatory requirements. The secure and regular structure of the repayment arrangement attracts more capital and lenders. These loans are perceived to be lower risk for lenders than personal unsecured loans for three reasons:

- 1) Utility consumers prioritize their energy bills above all other debts other than rent or mortgage payments²⁷;**
- 2) Where allowed, termination of utility service for non-payment of the loan are proven to lead to prompt restoration of arrears and timely payments; and**
- 3) Utility services are estimated to cost less once the retrofits are installed, so that the combined monthly payment is intended to be 'neutral' or at least not much higher than present monthly expenses.²⁸**

The Environmental Defense Fund lists these additional societal and economic benefits:

- No increased charges to taxpayers or ratepayers
- Green Job creation
- Emissions reductions
- Reduced program costs through a scalable platform and standardized processes
- Avoided costs as demand for new generation capacity is reduced²⁹

Federal policy makers, utility executives and their lending partners in 20 states as well as national advocacy organizations have made this case in many venues.

The purpose of this analysis is to explore any less-well-studied negative consequences that borrowers should be aware of and cautious about; it reviews risks not addressed in most discussions of the OBR/OBF policy options. Therefore, the detailed sections that follow explore very specific concerns which consumer advocates should address and bring to the attention of policy makers and regulators. Unanswered questions remain regarding potential negative consequences of participating in these programs because few have measurable results yet and many uncertainties about their structure, policies and impact are neither explored nor defined in law and regulation. It is designed to give

advocates an understanding of the open issues and a set of questions to answer as they participate in considering policy parameters set for OBR initiatives.

Consumer Risks from On-Bill Repayment

Program Practices

While some of the risks considered in this section are substantially higher for low- and moderate-income borrowers, all are potential threats to any residential customer. They fall into the categories of; erosion of utility-specific consumer protections, erosion of consumer loan protections, program design features that place ownership or the property transfer process at greater risk and, in general, reduction of access to energy supply because there is a negative consequence in terms of cost or regulatory barriers.

Erosion of Utility Consumer Protections from Disconnection

A serious risk to consumers is any increase in the probability of utility disconnection.³⁰ Lenders want the “security” of disconnection as a collection threat.

The California Public Utilities Commission’s proposed decision directs Investor-Owned Utilities to develop small-scale, non-residential OBF programs to test. Commission acknowledges regretfully that it does not have the authority to allow disconnection for non-energy charges; it advocates for new legislation allowing the practice.³¹

Only a handful of the current programs require that utilities and other lenders inform prospective borrowers that non-payment of the loan can lead to termination of utility service.³²

What consumer advocates need to find out:

- Whether disconnection is a possibility for nonpayment or partial payment of the efficiency improvement loans.
- Whether pre-existing disconnection regulations are being weakened as a condition of participating in the loan program including regulations regarding notice periods, budget payment plans, arrearage management terms and penalty or interest charges.
- Whether all conditions regarding implementing a disconnection comply with federal or applicable state debt collection practices.

- Whether there is a ‘fairness’ case to be made that, because now-standard consumer loan protections discussed in the following section and proven debt collection practices short of disconnection are not available to these borrowers , they should have additional, not fewer, protections from the extreme penalty of disconnection.

Erosion of General Consumer Lending Protections

The language or regulation authorizing each on-bill financing program is different, but very few carry consumer protections within them as far-reaching as a bank loan. The structure of the program affects whether the utility or the financial institution may be subject to federal consumer protection statutes that address procedures for the correction of errors on an account, protecting a consumer’s credit rating during dispute proceedings, and prohibiting discrimination in the selection of loan recipients, among others. However, many stricter state-specific laws are not referenced in the new enabling rules or statutes.

In OBR programs, many believe that utilities, because they act as the collection arm of third party, are required to comply with the federal Truth in Lending Act and the Equal Credit Opportunity Act. These laws spell out specific disclosure and notice rules that ensure that borrowers are aware of the terms of the loan. The utility would also have to follow applicable state laws unless exempted by the statute for this program, current programs lack such exceptions.

By contrast, OBF programs may not be subject to federal consumer protection laws which only apply to certain categories of lender because it may be difficult to determine who the owner of the funds is, especially if funds for these programs were collected as a surcharge on customers’ bills, or as part of a System Benefit Charge (SBC) program.³³ In these cases, the utility may be subject only to state protection laws, or in some cases, only to the protections clearly spelled out in the statute authorizing the on-bill lending.

Lack of Credit Standards

Utility customers are not denied access to OBR programs because of poor credit history or low credit scores. Some programs base access on the program to customers with a record of on-time payments for utility service; none require income qualification.³⁴

Many advocates for asset-development initiatives for low-wage working families applaud the opportunity to access home improvement credit not available through conventional lenders. Such loans can provide an opportunity to demonstrate responsible payment practices and build a credit history. On the other hand, these advocates' primary concern is to open opportunity to develop reportable payment information for building a formal credit history where none exists; their goal is to allow access to market lending that enables those with little credit history (known as those with "thin credit files") to build access to investments in important assets and human capital.³⁵ OBR programs vary in the degree to which they link payment records to credit reporting.

The low barrier to participation also increases the possibility that naïve borrowers may participate without having the full disclosure and protections associated with conventional home improvement loans. Such borrowers might face costs and risks they did not anticipate, especially if they assume there will be more energy cost reduction than is achieved. Advocates should consider whether there should be limits based on customer debt burden, income, home value, or even pre-treatment energy use. Put differently, these programs should not, by their design, create a new gateway for lenders in search of opportunities for making risky consumer loans to borrowers with shaky credit and uncertain financial capacity.

What consumer advocates need to find out:

- How are program participants chosen for participation in on-bill offerings?
- What credit standards are used for assessing ability to prepay? Are these criteria the result of public policy and/or regulation or are they created by the utilities and their lending partners? If so, is the practice uniform among all utilities and all lenders? If not, how are the policies and their variations disclosed?
- How do those standards compare to good practices or to statute governing predatory lending and its marketing?
- To what segments of the residential consumers is marketing targeted? i.e., is marketing likely to attract consumers that are the intended market or others who may face different risks by participating?

Disclosure of Terms and Penalties, Transparency

A number of statutes authorizing on-bill repayment programs do not specify disclosure of information that ensures the customer understands the efficiency program is a loan; many do not limit the sharing

of loan information; many do not give borrowers the chance to pre-pay without penalty; and most lack specifications requiring disclosure of how bills after the retrofit-upgrade will compare with prior utility bills.³⁶

The need for disclosure is a significant concern, especially with some lenders attempting to market on-bill financing as a “program” rather than a loan. Several states have included strong disclosure requirements in their framework so that consumers know they are taking out a loan and understand the interest rate and payment schedule and terms.³⁷ The strongest model is the legislation for New York which mandates such information and that it be ‘clear and conspicuous.’

Performance

Another major concern with the marketing of OBR programs is that marketing may not convey the fact that, while many people may see reductions in their monthly energy bills after the repayment period if not during, it is impossible to guarantee that result for all. It is even less likely that a high-impact investment that requires a significant expenditure will achieve bill neutrality during the life of the loan, which is typically much shorter than the life of high-impact measures such as insulation and high-efficiency heating or cooling systems.³⁸ There are likely to be inconsistencies with expectations of improvements and estimations of climate and estimates of homeowner behavior are approximate.³⁹ Larger loans for substantial retrofits may have a period of payback that is longer than the life of the loan. Also, if projected fuel prices are lower than estimated savings will be less. In either case, annual bills will not drop as much even after an improvement is paid off. Oregon is designing a program that will only make investments with guaranteed bill neutrality over the life of the loan for the low-income sector. However, it appears those loans may be too small to offer savings measures that are durable over a decade or more.⁴⁰

As stated by the California Public Utilities Commission, “While it would seem superficially appealing to offer loans along with energy efficiency projects that ensure that a customer’s total bill actually goes down, there are many factors besides the energy efficiency project that may determine whether that result actually occurs.”⁴¹ Without reduced, or at least stable, bills for utility service plus repayments, bills may be unaffordable.

The legislation enacted in New York requires in ‘clear and conspicuous’ terms that the company and lender inform the consumer: “That incurring such loans to undertake energy-efficiency projects may not result in lower monthly energy costs over time, based on additional factors that contribute to monthly energy costs.”⁴² However, other states’ authorizing statutes do not include such strong disclosure provisions.

What consumer advocates need to find out:

- Will potential borrowers be informed in unmistakable terms that their bills are not guaranteed to be lower after the loan is repaid?
- Will borrowers be clearly informed about what work or equipment is warranted and what is not, including energy performance or usage?

Grievance and Redress

It is important for consumers to have a neutral adjudicator in the event of a problem with their on-bill loan. Some states do not address the issue of contractor failure to deliver the promised services or lender violation of loan terms at all. Illinois authorizing legislation addresses the issue of dispute resolution by putting all of the responsibility on the consumer to resolve the dispute with the lender, offering no protections for legitimate grievances against lender or suppliers.⁴³ Disconnection typically triggers substantial on-bill penalties, including charges for reconnection and increased security deposits. It is not difficult to imagine a homeowner in a dispute over the quality of work delivered having no leverage against the non-performing contractor while the utility continues to bill for the work for which it has reimbursed the contractor and eventually disconnects the customer. The customer has no right to withhold payment for a faulty installation but could easily end up with a much higher energy bill than was historically the case.

In New York, however, the legislation requires the manager of the loan programs, state’s Energy Authority to set up a system to handle dispute resolutions.”⁴⁴

What consumer advocates need to find out:

- Do the disclosures to borrowers and the organization of loan servicing arrangements provide a reasonable and accessible process for directing complaints and winning satisfaction in the event of service, equipment or other failures of the transaction?

- Will the dissatisfied customer have a process by which his payments for poorly done or un-done work can be escrowed until the defects are remedied?

Debt Collection Practices

Disconnection as a penalty is arguably disproportionately harsh when compared to collection practices allowed for other consumer debt. The penalty for failure to pay a typical bank loan might be an adverse effect to one's credit score, difficulty obtaining credit in the future, and possibly the need to file for bankruptcy. The failure or refusal to pay an on-bill repayment loan could result in the shutting off of heat or cooling for extended periods in any season. No federal review of this argument with respect to the conformity of the practice with the Fair Debt Collection Practices Act has been undertaken.

Just as important, over the past decade or more, numerous OBR programs without a disconnection penalty have experienced very low default rates.⁴⁵ No evidence yet exists regarding the added value to lenders of the threat of utility disconnection.

What consumer advocates need to find out:

- Are OBR program lenders subject to federal consumer protection laws such as the Truth in Lending Act and the Fair Debt Collections Act?
- How do the disclosures and collection practices compare to those permitted under federal and state debt collection law?
- What regulations or statute apply?
- How do the allowable practices compare to the rights borrowers have with respect to other consumer or home improvement loans?
- How will the utility disclose the record of payment and non-payment in these programs to regulators?

Program Structures That Disadvantage Borrowers

Property Liens v. Unsecured Financing

Some programs allow lenders to attach liens either to the borrower's real property or to the home-improvement equipment supplied as added security on the loan. A lien is a non-possessory security interest, much like a mortgage, that essentially places a hold on the property and allows the holder to

keep the borrower from selling the property before the debt is repaid. If a borrower is unable to make the loan and utility payments and then, additionally, is unable to sell or refinance the property due to a lien, the debt will further compound. It is not impossible in such situations that a loan whether small or large, especially for a failed retrofit, can lead a cash-strapped borrower to a forced sale enforced by his utility. No state-wide programs are based upon this form of collateral, but many lenders require it for OBR loans. Only New York's legislation proactively disallows it.⁴⁶

What consumer advocates need to find out:

- Are lenders allowed to take liens as collateral and if so, how the utility program discloses this term to the borrower
- What does each lender associated with the utility OBR require the utility to do in enforcing a lien?
- What regulations or statute apply to that action?
- How do the allowable practices compare to the rights any lenders have with respect to other consumer or home improvement loans?

Ownership of the Loan

On-bill programs follow one of two paths in assigning responsibility for paying off the loan. Some programs' loans are debt owed by the original borrower.⁴⁷ If that individual moves, the repayment remains his or her responsibility. The advantage is that the individual who took out the loan is responsible for its repayment so there are fewer legal dilemmas for program administrators; there is no need to determine the legality of transferring a loan payment to a party that did not make the agreement; in fact, subsequent owners may well have very different energy usage patterns.⁴⁸

Loans that remain the borrower's responsibility have many risks. Individuals who move before paying off the entirety of the loan will be required to pay the remainder, whether or not the energy efficient upgrades can be physically moved to their new home, as in the case of a major appliance. This is especially risky for renters who often move more frequently.⁴⁹

The borrower-friendly path is to deem the loan a 'tariff', which means it is the responsibility of the utility meter account holder. A tariff runs 'in appurtenant,' meaning that subsequent occupants of the same property will pay the cost of the upgrade on their utility bills. The tariff concept is that the

individual receiving the benefit from the energy efficient upgrades should be paying off the loan. New programs in Kentucky, Oregon and New York use a tariff model. These three state programs require a form of notification to be given to subsequent homeowners or renters. This design has inadequacies as well.⁵⁰ When a borrower sells the house, they transfer the on-bill tariff. Depending on the property laws of the particular state, new legislation may also be necessary to enable loans to transfer to a party not privy to its making.⁵¹ Without more experience, it remains unknown whether these tariffs will cause problems for homeowners at time of sale.

What consumer advocates need to find out:

- Does the loan stay with the meter or the individual?
- Is disclosure on this issue required, clear and appropriate to let borrowers know their future obligation if they move?
- How do sellers, mortgage lenders and the utility inform potential home buyers of the on-bill loan.

Risks for Low-Income Consumers

While the above risk factors in the design of OBR programs affect all small consumers, some of the features of the programs discussed are substantially higher for lower-income households because of differences in energy usage patterns and differences in borrowing experiences that are directly associated with income levels.

While the affordability of monthly payments as a share of all monthly household expenses is an obvious risk factor, so are differences in household tenure and mobility patterns, in households' experience with managing credit and in the degree to which participation in OBR may have on nullifying rates, public sector programs and consumer protections that are now available to eligible households.

Affordability

Advocates for low-income families assess whether a cost is affordable by studying its effect on a household's ability to meet the costs of all basic necessities, primarily housing including energy and water, food, basic transportation costs, basic clothing and some health expenditures. One reason

efficiency investments are a goal of these advocates is that they may reduce the share of household income devoted to energy and make more money available to meet more or basic needs.

Energy Cost Burden: At present, average annual household utility and/or bulk fuel bills continue to require between 11% and 15% of the annual income of the population with income under 150% of the Federal Poverty guideline (FPG).⁵² The percent of income is referred to as energy 'burden'. The range of estimates reflects changes in weather and prices that can cause energy burden to vary up to 4% of a family income for the entire year; yet these phenomena are impossible for a family to predict and budget for. In 2011, there were 24 million households in poverty.⁵³ Nearly twice as many households have incomes that qualify them to receive federal Low-Income Home Energy Assistance and Weatherization Assistance where it is available. As a group, the eligible lower-income households' usage and bills are typically 20% lower than those of better-off consumers,⁵⁴ but the share of income needed to cover their energy costs is almost 3 times higher. For the households in poverty, usage is 40% less but energy bills demand nearly 25% of income on average. By contrast, the average percent of annual income spent by households with incomes too high to qualify for public programs averages 4%.⁵⁵

Impact and Vulnerability: The burden, or percent of all resources, determines the impact of any addition to a monthly payment obligation. If an energy bill rose by \$50 a month, it would consume an additional 6% of the incomes of disabled and elderly participants in the Supplemental (Social) Security Income program who make up a substantial share of those eligible for federal bill payment assistance; however, it would require only 1/10th of 1 percent of the monthly income of the consumer earning \$75,000 yearly. The impact of the same increase, \$50, is dramatically different for the two consumers.

Many low-income consumers cannot afford all their energy bills in a given year, especially those who are not on a level payment plan. This means that even OBR programs that guarantee bill neutrality may not be 'safe' for the lowest income households. Census data collected between 1997 and 2006 shows that about 9% of American utility consumers in all income levels combined reported they could not pay a monthly energy bill because of lack of funds,⁵⁶ and half of them had incomes below 150% of the FPG.⁵⁷ Additional data show the late-paying households were predominantly working families with children, and were likely to be experiencing several other hardships at the same time; the most commonly-reported consequences were inability to pay not only the utility bill but also inability to pay

the rent on time or to buy enough food to feed children 3 meals daily. About a third of those unable to pay suffered a disconnection of services.⁵⁸

The impact of disconnection of service is similarly disparate. Reconnection typically requires steep penalty payments, making the elapsed time to reconnection longer for lower-income households and the hardships associated with lack of power or gas heat more intense. The lowest income customers are also disproportionately renter households consisting of single working parents and their children.

Nevertheless, the vast majority of the low-income households made their on-time payments in spite of the high burden on their resources. Advocates and those managing the public bill-assistance programs promote tools for distinguishing the “cannot pay” customers from those who are careless or worse- the “will not pay” when they can afford to pay. The issues raised in this section focus on the “cannot pay” customers.

Credit Records and Scores

Because OBR programs do not screen for credit risk with conventional tools, lenders cannot assess the risk that any one customer may fall into the ‘can’t pay’ category. Even a good payment record over a 6-12 month period may not indicate a future ability to maintain the payment stream no matter how willing the customer may be. Low-income working households are far more vulnerable to income fluctuations than are salaried workers with benefits that include leave in the event of illness or emergency or than retirees and others on fixed incomes. Job insecurity, lack of affordable health insurance and absence of savings to cover the expenses of a natural or family crisis all place their economic stability at risk. For these households, the importance of having clear information about the OBR loan, the bills that will result following the improvements and after the loan is repaid, the customer’s rights in the event of a grievance and about the risks and penalties for non-payment cannot be overstated. Properly informed, they will assess their interests appropriately.

What consumer advocates need to find out:

- Is the program being marketed in a way that allows lower-income customers to assess their personal risk of being unable to pay and of the penalties involved as compared to benefits of the energy savings?
- How will the program or lender determine whether the lower-consumer is at risk of being unable to pay? Will any of these factors be considered: currently unaffordable bills? potential

for a higher bill during the loan repayment period? potential for a higher bill because of new fixed charges that do not appear in current bills?

- What are appropriate, non-discriminatory screening criteria to validate future ability to pay without incurring a disproportionate risk of disconnection? In South Carolina, the Touchstone pilot program required 2 years of on-time payments, a fairly restrictive threshold test that may well have succeeded in deterring at-risk customers.⁵⁹
- What protections can be added to the program to reduce, rather than increase, the risk of disconnection for vulnerable families participating?
- What are legitimate marketing approaches to this population, i.e. approaches that do not minimize the risks of taking the loan?
- Are there safeguards allowing borrowers who demonstrate a hardship to delay and reschedule loan payments? Are there protections from unsatisfactory retrofit work? From loan service practices that violate the agreement terms?

Mobility

As a group, renters move more often than homeowners. Most low-income households with permanent housing, including 59% of those with incomes up to the FPG, rent apartments, mobile homes or single-family houses. They also move more often than renters who are not low-income. In fact, in 2009, the American Housing Survey showed nearly half of renters in poverty had moved at least once in the past year compared to 37% of all other renters.⁶⁰ By contrast, fewer than 10% of all homeowners moved in 2009.

It is unlikely the frequently-moving population would enjoy long-term benefits from the investment, and therefore it is also nearly certain that an obligation that followed the borrower to a new location would unfairly burden him or her.

Damage to Energy Assistance Benefits and Regulatory Protections

The federal Low-Income Home Energy Assistance program (LIHEAP) and rate-payer funded bill discount programs in many states provide revenue for utilities that allows them to lower the bills and energy burden of income-eligible customers. States have flexibility in setting the rules for LIHEAP payments, but at least some states when calculating the benefits exclude from LIHEAP coverage any charges on the bill that are not for energy services.⁶¹ In other words, a LIHEAP participant who borrows under an OBR program may achieve 'bill neutrality' if the energy savings and loan payments are equivalent, but can still be required to make a much larger out-of-pocket payment because the LIHEAP benefit will drop when calculated in consideration only of the [now-reduced] energy services charges. This

requirement puts the borrower at greater risk of default and termination and also costs the utility revenue from the federal -state program.

Similarly, if ratepayer-funded discounts are calculated based on energy charges, a typical design, the eligible customer's bill will rise disproportionately when the not-discounted loan payments replace the discounted service charges.

Many states have established lower penalties and fees for disconnection for low-income customers which do not clearly apply if the disconnection is because of non-payment of the OBR amount.

What consumer advocates need to find out:

- Would participating in an OBR loan reduce the share of utility bills otherwise covered by assistance or discounts for low-income customers under state program rules or rate regulations? If so,
 - What would be the impact on the energy burden of low-income participants in OBR financing?
 - How would the risks of disconnection or other hardships change as compared to before they took the loan?
- Is the potential risk clearly disclosed before the loan is made?

In summary, lower-income customers face two-categories of elevated risk as compared to other OBR potential participants: a higher risk of incurring a more costly utility bill because the benefits of programs and protections in which they participate will drop more than their total bill drops and a higher risk of being unable to pay bills that stay at the pre-loan level which was never easily affordable.

All parties in the design and marketing of OBR loans should ensure that the framework does not materially raise the energy burden of any household in the near- or the long-term and that the design does not put the most vulnerable customers at greater risk of unaffordable bills and disconnection if they participate. These are difficult issues to resolve but, unless these tests can be met, the rationale for marketing OBR loans to low-income customers is weak at best. Consumer advocates should insist on a thorough analysis before the low-income market is included in a program.

Conclusion

On-bill financing and repayment programs offer easy access to very low-cost financing for home improvements that are urgently needed. Yet, there are worrisome unanswered questions about

whether the design of the programs for individual utility residential customers protects borrowers from a too-familiar market of easy credit offerings with poorly-understood payment terms and inadequate provisions governing notice, dispute resolution and loan servicing standards which carry draconian penalties for non-payment.

Policy makers and utilities partnering with lenders must ensure borrowers are well-informed and are protected at least as well as they are when taking out an unsecured consumer loan from a regulated lender. Participation in OBR financing should not dilute or eradicate protections afforded utility consumers with respect to their bills and their rights, including rights related to disconnection of service. It is unclear whether all the recently established OBR initiatives meet these tests; in fact, it appears many do not.

There are greater risks to lower-income borrowers than to others, not only because they may have less ability to sustain regular payments but also because in most states they have access to assistance and special rate protections that OBR participation could jeopardize. Further, the benefits to low-income borrowers are unproven; these households use less energy than the average American household and move far more frequently. The benefit/cost calculation of small loans' placement and servicing costs compared to the durable efficiency gains for the household or utility system are questionable.

As OBR financing programs increase in popularity, advocates for low-income weatherization and housing affordability should ally with experts on fair lending practices. Together they can better craft financing designs that carry the same or greater protections as a bank loan and as utility regulations that protect residential and/or low-income customers with respect to rate design, bill collection and shutoffs.

The most consumer-friendly practices include:

- Disconnection is not permissible for non-payment of the loan if the utility service portion of the bill is paid. Instead, the lender should have the same collection tools as regulated originators of consumer loans;
- Associating the loan obligation with the meter on the property where the retrofits are installed with clear information for subsequent account holders regarding the transfer of the balance of the loan;
- Consumer disclosures, including about risks in the event of non-payment or of leaving the property and about the post-retrofit bills that are equivalent to the plain-English language notices required for other consumer credit offerings;

- Procedures for fairly responding to consumer grievances and complaints;
- Consideration of on-time utility payment records over several peak seasons to indicate whether the risk of a higher bill during the repayment period may lead to inability to pay and loss of energy service;
- Targeted low-income consumer disclosure that ensures borrowers know exactly how much bill assistance or regulatory protection will be available to them if they participate and know about any risks they face;
- Requirements for coordination with utility, public and private organizations providing energy assistance and efficiency services to reduce duplication and increase protections for these vulnerable customers, and
- Marketing material content, design and targeting policies that implement all the above protections.

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Endnotes

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³ Matthew H. Brown & Beth Conover, *Recent Innovations in Financing for Clean Energy*, Southwest Energy Efficiency Project, 17, (Oct. 2009), available at http://www.swenergy.org/publications/documents/Recent_Innovations_in_Financing_for_Clean_Energy.pdf.

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- ⁴Brad Copithorne & James Fine, *On-Bill Repayment: Unlocking the Energy Efficiency Puzzle in California* at 6 (2011), available at <http://www.edf.org/sites/default/files/On-Bill%20Repayment-Unlocking-the-Energy-Efficiency-Puzzle-in-California.pdf>.
- ⁵ *Hearing on the FY 2013 Budget Request for DOE: Hearing before the Subcommittee on Energy and Water Development of the Senate Committee on Appropriations*, 112 Cong. (Mar. 14, 2012) (testimony of Sec. Steven Chu) <http://www.appropriations.senate.gov/webcasts.cfm?method=webcasts.view&id=431fc3c9-9a6e-442d-bac8-fe63d7a9fddf>.
- ⁶ Copithorne & Fine, *supra* note 3, at 7.
- ⁷ *Proceeding on Motion of the Commission Regarding an Energy Efficiency Portfolio Standard (EEPS)*, State of New York Public Service Commission, 7-9 (Dec. 2008), available at http://www.nclc.org/images/pdf/energy_utility_telecom/obf/WGVI-On_Bill_Financing_Final_Report.pdf.
- ⁸ Copithorne & Fine, *supra* note 3, at 7.
- ⁹ See Martha Amram, Penny Angkinand & Betsy Zeidman, *Financing the Residential Retrofit Revolution*, Milken Institute Financial Innovation Lab Report 27 (2010), available at http://www.milkeninstitute.org/pdf/FILab_Res_Retrofit_April_20.pdf; *Citi Conference on EE Financing*, Harcourt, Brown & Carey Energy & Finance (last visited Nov. 14, 2012) <http://www.harcourtbrown.com/citi-conference-on-ee-financing/>.
- ¹⁰ See Lynn Sadler, *SB 998 (de Leon) – Energy efficiency, renewable energy, and distributed generation on-bill repayment programs memorandum*, California Public Utilities Commission 4 (May 22, 2012) http://www.cpuc.ca.gov/NR/rdonlyres/EEB13C04-AC82-4E70-8197-2F534451B8C5/0/CPUC01166978_SB_998_Leg_Memo_52412.pdf.
- ¹¹ Copithorne & Fine, *supra* note 3, at 7-8.¹² *Id.*
- ¹³ See e.g., *Proceeding on Motion of the Commission Regarding an Energy Efficiency Portfolio Standard (EEPS)*, *supra* note 6 at 26-27; James M. Van Nostrand, *Legal Issues in Financing Energy Efficiency: Creative Solutions for Funding the Initial Capital Costs of Investments in Energy Efficiency Measures*, GEO. WASH. J. ENERGY & ENVTL. L. 12-13 (2011).
- ¹⁴ *Id.* Also Merrian C. Fuller, *Enabling Investments in Energy Efficiency...supra* note 2. (2009); Also Brad Copithorne & James Fine, *On-Bill Repayment: Unlocking the Energy Efficiency Puzzle in California* at 8 (2011).
- ¹⁵ *Proceeding on Motion of the Commission Regarding an Energy Efficiency Portfolio Standard (EEPS)*, *supra* note 6 at 26-27.
- ¹⁶ Brad Copithorne & James Fine, *On-Bill Repayment: Unlocking the Energy Efficiency Puzzle in California* at 8 (2011).
- ¹⁷ California, Hawaii, Illinois, Kentucky, Michigan, New York, Oregon, and South Carolina
- ¹⁸ See MCL 460.1045 (2008); 220 Ill. Comp. Stat. Ann. 5/19-140 (West 2009); O.R.S. § 470.660 (2009); Ann.Cal.Pub.Util.Code § 2842.4 (2009); S.C. Code Ann. 1976 § 58-37-50 (2010); HRS § 269-125 (2011); N.Y. Pub. Serv. Law § 66-m (McKinney 2011).
- ¹⁹ MCL 460.1045 (2008).
- ²⁰ Ann.Cal.Pub.Res.Code § 25943 (2009).
- ²¹ Proposed Decision of ALJ Farrar, 09-11-014 California Public Utilities Commission at 19 (Mar. 20, 2012).
- ²² *Id.*
- ²³ *Memorandum in Support A.11427/S.7565*, Public Utility Law Project of New York, Inc. 1 (June 21, 2010).
- ²⁴ *Proposed Rule Energy Efficiency and Conservation Loan Program*, Rural Utilities Service 77 FR 43723, 43723 (July 26, 2012).
- ²⁵ In 2011, the RUS gave a direct loan to a coalition of South Carolina cooperatives for a pilot program.
- ²⁶ <http://www.edf.org/energy/obr>. The website of the Environmental Defense Fund, an advocacy organization that plays a major role in refining the concept of On-Bill financing and mobilizing resources and policy changes for implementation.
- ²⁷ The US Census Bureau's Survey of Income and Program Participation tracked measures of adult material well-being in long-term cohorts of respondents whose experiences are tracked over time. One indicator is an inability to afford to meet bills from basic needs, and inability to pay utility bills timely was an indicator tracked. The official report on the group tracked beginning in 1999 is found in Chapter 4 of Ouellette, Tammy, Nancy Burstein, David Long, and Erik Beecroft 'Measuring Material Hardship in the SIPP' Measures of Material Hardship: Final Report at Chapter 4. <http://aspe.hhs.gov/hsp/material-hardship04/ch4.htm#Ch4C>. as cited in
- ²⁷For example, the NYSERDA administered program in New York is able to offer on-bill loans with a 2.99 percent interest rate, as opposed to the 3.99 percent financing it can offer for unattached energy efficiency loans through its Green Jobs Green New York financing program.
- ²⁹ <http://www.edf.org/energy/obr>

³⁰ Olivia Wein and John Howat, *Reply Comments of the National Consumer Law Center on the Proposed Decision of Administrative Law Judge Farrar's Guidance on 2013-2014 Energy Efficiency Portfolios and 2012 Marketing, Education, and Outreach* at 1 (Apr. 16, 2012).

³¹ "... at this time we do not have the legal authority to allow the utilities to initiate collection actions for non-payment of portions of the utility bill not related to provision of utility services, and that could lead to disconnection," the proposed decision states. However, California's SB 998 which failed to pass by the end of the legislative session even with backing from the Public Utilities Commission would have given the Public Utilities Commission that authority. "The bill would authorize the commission to require an electrical corporation or gas corporation to treat any resulting shortfall in payment for electric or gas service consistent with the rules established by the commission for a customer's failure to pay for electric or gas service.," (emphasis ours) SB 998 states.

³² As stated in New York's McKinney's Public Authorities Law § 66-m(F): "Prior to or at the closing of each loan made pursuant to this section, the Authority shall cause a notice to be provided to each customer receiving such loan stating, in clear and conspicuous terms: That the on-bill recovery charge will be billed by such customer utility company and that failure to pay such on-bill recovery charge may result in the customer having his or her electricity and/or gas terminated for non-payment, provided that such utility company follows the requirements of article two of the public service law with respect to residential customers."

³³ *Proceeding on Motion of the Commission Regarding an Energy Efficiency Portfolio Standard (EEPS)*, *supra* note 6 at 7-9.

³⁴ See *Id.* at 16; also *On-Bill Financing: Customer and Contractor Handbook*, San Diego Gas & Electric 2, available at <http://www.sdge.com/sites/default/files/documents/1193259304/OBFHandbook202012.pdf>; *New York Home Performance with ENERGY STAR Financing Program*, Energy Finance Solutions, <http://www.energyfinancesolutions.com/main/homeownersnyfour>.

³⁵ Turner, Michael et. al., [Give Credit Where Credit Is Due: Increasing Access To Affordable Mainstream Credit Using Alternative Data](#). Monograph. Political And Economic Research Council & The Brookings Institution Urban Markets Initiative, Washington, DC, 2006 http://www.brookings.edu/~media/research/files/reports/2006/12/communitydevelopment%20turner/20061218_givecredit.pdf

³⁶ See 220 Ill. Comp. Stat. Ann. 5/16-111.7 (West 2011), 220 Ill. Comp. Stat. Ann. 5/19-140 (West 2009), S.C. Code Ann. 1976 § 58-37-50 (2010).

³⁷ Legislation in South Carolina, as stated in Code 1976 § 58-37-50, "Any agreement permitted by subsection (B) must state plainly the interest rate to be charged to finance the costs of energy efficiency and conservation measures." Likewise, in Oregon, O.R.S. § 470.660 states that companies must, "Provide a clearly identifiable line item or separate statement in the utility bill that shows the energy efficiency and sustainable technology loan repayment amount..." Even stronger is the legislation in New York, which mandates that such information be "clear and conspicuous"

³⁸ A fuller discussion of these concerns is in Merrian C. Fuller, *Enabling Investments in Energy Efficiency: A Study of Energy Efficiency Programs that Reduce First-Cost Barriers in the Residential Sector* (2009) *supra* note 2 at 22.

³⁹ Olivia Wein and John Howat, *Reply Comments of the National Consumer Law Center on the Proposed Decision of Administrative Law Judge Farrar's Guidance on 2013-2014 Energy Efficiency Portfolios and 2012 Marketing, Education, and Outreach* at 4 (Apr. 16, 2012).

⁴⁰ Meg Power interview with Dan Elliott, Policy analyst, Oregon Housing and Community Services Department, January 7, 2013.

⁴¹ Proposed Decision of ALJ Farrar, *supra* note 20 at 123.

⁴² N.Y. Pub. Serv. Law § 66-m (McKinney 2011).

⁴³ As codified in 220 ILCS 5/19-140(c)(5), "A loan issued to a participant pursuant to the program shall be the sole responsibility of the participant, and any dispute that may arise concerning the loan's terms, conditions, or charges shall be resolved between the participant and the lender."

⁴⁴ As stated in New York's McKinney's Public Authorities Law § 66-m(F)(4): "...it is the sole responsibility of the authority to handle consumer inquiries and complaints related to the operation and lending associated with the program, provided further that the authority shall provide a mechanism to receive such consumer inquiries and complaints"

⁴⁵ Merrian C. Fuller, *Enabling Investments in Energy Efficiency: A Study of Energy Efficiency Programs that Reduce First-Cost Barriers in the Residential Sector* (2009), *supra*, note 2 at 48.

⁴⁶ *On-Bill Financing Program Frequently Asked Questions*, NYSEDA <http://www.nyserda.ny.gov/en/Statewide-Initiatives/On-Bill-Recovery-Financing-Program/FAQ.aspx>.

⁴⁷ Catherine J. Bell, Steven Nadel & Sara Hayes, *SUPRA*, NOTE 1 AT 4

⁴⁸ Olivia Wein and John Howat, *Reply Comments of the National Consumer Law Center on the Proposed Decision of Administrative Law Judge Farrar's Guidance on 2013-2014 Energy Efficiency Portfolios and 2012 Marketing, Education, and Outreach*, 09-11-014 California Public Utilities Commission 2 (Apr. 16, 2012).

⁴⁹ W. Jean Yeung and Sandra L. Hofferth, *Family Adaptations to Income and Job Loss in the U.S.*, 19 JOURNAL OF FAMILY AND ECONOMIC ISSUES 255, 255 (1998).

⁵⁰ Bell, Nadel & Hayes, *supra* note 1, at 5.

⁵¹ Wein & Howat, *supra* note 29 at 2.

⁵² Among the most recent in a series of studies of low-income household energy burden in the past five years are: Eisenberg, Joel F., *Weatherization Assistance program Technical Memorandum*, Oak Ridge National Laboratory, 2010 at http://weatherization.ornl.gov/pdfs/ORNL_TM-2010-66.pdf; and the FY 2009 version of the Low-Income Home Energy Assistance Program 's data 'Notebook' prepared by APPRISE, Inc. in 2011 <http://www.acf.hhs.gov/programs/ocs/resource/liheap-2009-home-energy-notebook>, Table A-3b, p 72; and Meg Power, http://www.opportunitystudies.org/repository/File/energy_affordability/Forecast_Burdens_08.pdf

⁵³ The Census Bureau annual report on Poverty, Income and Health Insurance does not provide counts of households, rather than families, by poverty status. Households are the unit that jointly consumes energy and other commodities in a home. However, these statistics can be derived for 2009-2011 from the data tables presented in Suzanne Macartney and Mykyta, Larissa, 'Poverty and Shared Households by State: 2011' *American Community Survey Briefs* November 2012 ACSBR/11-05. <http://www.census.gov/prod/2012pubs/acsbr11-05.pdf>

⁵⁴ Power, Meg 'The Burden of FY 2008 Residential Energy Bills on Low-Income Consumers' Washington, DC. March, 2008. The comparison between those with incomes below the FPG and all others who qualify as eligible for federal energy assistance programs is shown in Chart 3 on page 4.

⁵⁵ *Id.* Table 3, page 9.

⁵⁶ The most recent government report summarizing these and other indicators of adult well-being is Ouellette, Tammy Nancy Burstein, David Long, and Erik Beecroft *Measures of Material Hardship: Final Report*. U.S. Department of Health and Human Services, Office of the Assistant Secretary for Planning and Evaluation Washington, DC. April 2004 <http://aspe.hhs.gov/hsp/material-hardship04/>. Table 4.5 shows the higher incidence among single-parent families

⁵⁷ Power, Meg, 2004 presentation of an analysis of the Census data on measures of adult well-being. 'Making Ends Meet' at <http://www.opportunitystudies.org/energy-affordability/burden/>

⁵⁸ Ouellette *et. al.* Table 4-14

⁵⁹ Ecova. "Help My House Pilot Program Summary Report." *The Electric Cooperatives of South Carolina*. 22 Oct 2012. Web. 23 Jun 2012. <http://www.ecsc.org/Libraries/Energy_Information/Help_My_House_Pilot_Program_-_Initial_Summary_Report_June_2012.sflb.ashx>

⁶⁰ All these statistics are computed from <http://www.census.gov/prod/2011pubs/h150-09.pdf> table 4-10. These data for 2009 are nearly the same as the data in the annual table with the same number in the reports for the four previous years.

⁶¹ Unpublished memo to the authors. 8/16/2012 Shirley Bergert, "Energy assistance in CT currently pays toward the primary heating cost of eligible consumers (up to 60% SMI), meaning a single vendor, either a utility or energy company. If some of a heating bill is shifted to loan repayment, low income consumers could lose needed energy assistance unless the energy assistance program is required to recognize the loan repayment as payment of a heating bill that is eligible for energy assistance coverage. This can get complicated if the loan repayment is on, for example, the electric bill and the primary heat source is not electric (e.g., gas or oil), and would require a significant change in the historic way CT has handled energy assistance, requiring DSS, OPM and legislative approval, cooperation of the Community Action Agencies with which DSS contracts to administer the program, and probably some significant IT modifications on the part of administering agencies and the utilities."