

# Towards Understanding the Role of Price in Residential Electricity Choices: Evidence from a Natural Experiment\*

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## Abstract

We examine a choice setting in which residential electricity consumers may respond to non-financial incentives in addition to prices. Using data from a natural field experiment that exposed some households to a change in their electricity rates, we find that households *reduced* electricity usage in response to a contemporaneous decrease in electricity prices. This provides clear evidence that other factors – potentially encompassing non-monetary and dynamic considerations – can influence consumer choice, and even dominate the static price response in some cases. A comprehensive understanding of household behavior in energy markets is essential for the effective implementation of market-based energy and environmental policies. The documentation of our result and others like it is a necessary step in achieving such an understanding.

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# 1 Introduction

Most economists, including ourselves, favor market-based approaches to addressing energy and environmental issues. The theoretical attractiveness of such instruments relies partly on being able to predict how consumers will respond to prices. But a growing body of empirical evidence suggests that within the energy choice setting, consumer behavior can be affected by a number of non-pecuniary factors in addition to prices. Further, some consumer decisions today will affect energy requirements in subsequent months and years, implying that anticipated prices far into the future may also play a role. Understanding the full context in which consumer choices are made is crucial for designing market-based instruments that can achieve efficiency in energy markets and broader environmental goals cost-effectively.

In this paper, we document an instance in which households did not respond to a retail electricity price intervention as economists would generally predict. Specifically, the intervention *lowered* the price of electricity for a number of months, but we find that households responded to it by *decreasing* their electricity usage in those months. Our empirical setting offers a unique opportunity to test how consumers respond to contemporaneous prices when other considerations may also be important, and we find conclusively that in this instance the other drivers of behavior dominated. While we are left to speculate about the precise mechanisms that were at play, our results suggest that there may be risk in adhering too ideologically to price interventions in terms of missing policy goals or achieving them only imperfectly or inefficiently. An assertion that static price incentives always work can be disproven by the counter-example we provide.

Our findings may not be entirely surprising. The theory of “bounded rationality” has long predicted that it may be rational for consumers to be imperfectly informed or to not deploy full cognitive effort in the face of information acquisition or cognition costs (Simon (1955)), leading to outcomes that appear sub-optimal. More generally, people may be mo-

tivated by intrinsic forces in addition to extrinsic (e.g. financial) incentives. This concept, already widely accepted by psychologists and sociologists, has recently entered the economics domain in Benabou and Tirole (2003) and others. In the residential electricity choice setting, non-monetary incentives such as moral license or pressure to conform to social norms can dominate financial incentives. Voluntary enrollees in carbon offset and green electricity programs increase their electricity consumption despite also facing higher prices (Harding and Rapson (2013) and Jacobsen, Kotchen, and Vandenberg (2012)), and customers informed of their neighbors' electricity usage respond by using less themselves (Allcott (2011)). Altruism and green identity also play important roles, with environmental concerns becoming a relevant aspect of consumer decisions (as in Kotchen and Moore (2007)).

In addition to the significant potential for such non-financial motivations to influence electricity choices, consumers grapple with the complexity of the setting, which could reduce the effectiveness of price signals. Features such as multi-tiered pricing structures (as explored by Reiss and White (2005)) or noisy signals about consumption may limit customers' ability to respond to prices. Consumers facing an increasing-block electricity rate structure appear to respond more to average price than marginal price (Ito (forthcoming)), and high frequency information about real-time consumption increases the price elasticity of electricity demand (Jesoe and Rapson (forthcoming)). Interventions that make prices or expenditure more salient may meaningfully influence household electricity usage: for example, residential consumers have been shown to conserve electricity immediately after receiving their electricity bill (Gilbert and Graff-Zivin (2013)).

These results suggest that the price elasticity of residential electricity demand may depend on several very specific aspects of the various settings in which different consumers make their electricity choices. Unobserved variation in the presence of these factors within and across different populations may therefore partially explain the variety of estimated price elasticities that have been reported in the literature (e.g. Alberini, Gans, and Velez-Lopez (2011), Fell,

Li, and Paul (forthcoming), Reiss and White (2005), Ito (forthcoming)). A sensitivity of price responsiveness to unobserved factors may also make broad policy recommendations drawn from a limited number of program evaluations misleading. For example, Faruqui and Sergici (2010) provide a meta-analysis of a number of price interventions and conclude that price-based policies are an effective means to achieve desired reductions in usage. However, while their findings may indicate that prices often work, they do not imply that prices always work, and give regulators limited guidance on how future interventions can be designed most effectively.

In this paper, we present a case in which a price change did not work as expected, in the sense that the implied short-run price elasticity is large and of the wrong sign. This surprising result is well-identified by a natural experiment that we partnered with an electricity distribution company (EDC) to evaluate. The EDC, located in the northeast US, implemented a large-scale mandatory residential time-of-use (TOU) program that forced households to switch irrevocably from a flat rate tariff to a TOU tariff after breaching a monthly usage threshold.<sup>1</sup> The setting gives rise to a regression discontinuity framework in which we compare outcomes of households just above the usage threshold to those of households falling just below the cutoff. Due to customers' inability to perfectly control monthly usage, in the neighborhood of the usage threshold assignment to the TOU rate is as good as random. The large-scale deployment of the program exhibits a high density around the threshold, creating a large sample of treatment and control households on which we examine responses to the change in the price of electricity induced by the intervention.

In the first summer months of the program in 2008, TOU rates were low relative to the flat rate alternative. Whereas the standard formulation of TOU prices is for the on-peak rate

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<sup>1</sup>TOU electricity pricing divides electricity use into two blocks according to the time of day at which electricity is consumed, and applies a higher rate to the block corresponding to historically high-cost times. It is a small step towards aligning retail electricity prices with marginal production costs. It is also the most common corrective measure used by electricity regulators to achieve such an alignment, due largely to the crucial advantage of being easy for consumers to understand and, in principle, respond to.

to be substantially higher than the flat rate and the off-peak rate substantially lower, in our setting TOU households faced on-peak rates in June to September of 2008 that were either lower than the relevant flat rate, or only slightly higher.<sup>2</sup> Off-peak rates were correspondingly even lower. The static financial incentives for TOU households are clear: total electricity use in those months – regardless of substitution patterns across on-peak and off-peak hours – should increase.

We find the opposite: TOU customers *reduced* total electricity consumption, as measured by our estimates of the treatment effect at the threshold. It is thus clear that households responded to other incentives in addition to contemporaneous prices, and that these other incentives dominated. Their choices could be rationalized by allowing for various dynamic considerations and behavioral psychology factors. We discuss these but do not perform formal tests, which our data cannot support. Nevertheless, the simple documentation of this result is an important step towards understanding energy demand behavior more comprehensively. Such an understanding will be invaluable in designing improved market-based interventions that incorporate factors complementary to price incentives and avoid others that might dull price incentives.

The paper is organized as follows: in Section 2 we review a price-based static optimization model and its predictions regarding electricity demand, which we contrast our results with throughout; Section 3 describes the program design, which forms the basis for our empirical setting; we explain how the setting can be viewed as a natural experiment and provide a description of our data in Section 4; treatment effects are reported in Section 5 and interpreted in Section 6; and Section 7 concludes.

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<sup>2</sup>Customers may purchase the generation component of their electricity services from either our EDC partner or an alternate supplier. This choice affects the relative on-peak and off-peak prices (the “TOU gradient”). In the discussion below we demonstrate why this does not affect our conclusions.

## 2 Theoretical Framework

We begin by reviewing a static optimization model of short-run household electricity demand by time of use. Our purpose is twofold: to clarify what is meant by the overall price of electricity in the time-of-use setting; and to lay the groundwork for demonstrating the limits of static price incentives – which are the sole focus of this particular model – in predicting behavior other than the standard inverse relation between price and usage.<sup>3</sup>

Following Hausman, Kinnucan, and McFadden (1979), we specify a household’s monthly utility function as

$$U = U(x^{on}, x^{off}, \mathbf{y}), \quad (1)$$

where  $x^{on}$  and  $x^{off}$  are the household’s monthly on-peak and off-peak electricity usage, respectively, and  $\mathbf{y}$  is a vector of all other goods.<sup>4</sup> We then make a weak separability assumption so that utility can be characterized as

$$U = W(f(x^{on}, x^{off}), y), \quad (2)$$

where  $f(x^{on}, x^{off})$  represents a homogeneous of degree one Hicksian aggregation of on-peak and off-peak electricity consumption, and  $y$  is the aggregate outside good, i.e. a Hicksian composite of all the goods in  $\mathbf{y}$ . Normalizing the price of  $y$  to unity permits  $y$  to be interpreted simply as expenditure on all goods besides electricity.

The weak separability condition allows the household’s monthly maximization problem to be decomposed into two levels. The expenditure level represents the household’s choice

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<sup>3</sup>The framework, presented in detail in Aigner and Poirier (1979), was first used by Hausman, Kinnucan, and McFadden (1979) and Caves and Christensen (1980) to estimate the on-peak and off-peak price elasticities corresponding to TOU experiments in Connecticut and Wisconsin, respectively.

<sup>4</sup>An important assumption underlying this utility specification is that the stock of electricity-using appliances is fixed. Therefore,  $x^{on}$  and  $x^{off}$  should be thought of as derived electricity demand based on demand for household services that use these appliances and the times of day that the household prefers to consume such services.

of how much to spend on total electricity usage, where the remainder of its (fixed) income is spent on the aggregate outside good. The allocation level describes the household's choice of how to allocate electricity consumption across on-peak and off-peak hours for given total electricity expenditure, which depends only on electricity rates.

The choice of total electricity usage,  $X \equiv x^{on} + x^{off}$ , will depend on an aggregated price of electricity  $p$  given by

$$p = sp^{on} + (1 - s)p^{off}, \quad (3)$$

where  $s$  is the share of on-peak usage in total usage as determined in the allocation level of the maximization problem.<sup>5</sup> The overall price of electricity is therefore simply the consumption-weighted average of the on-peak rate  $p^{on}$  and the off-peak rate  $p^{off}$ .

From the perspective of the expenditure level of the maximization problem, total electricity demand,  $X$ , can be affected by changes in the peak and off-peak rates through two channels. First, changes in the individual rates change the price of electricity,  $p$ , both directly and through the determination of the on-peak share,  $s$ , in the allocation level of the problem. These changes in  $p$  are associated with the usual income and substitution effects on  $X$  and the aggregate outside good as in any two-good framework. Second, changes in the individual rates can induce ancillary substitution effects between the aggregate outside good and the individual levels of peak and off-peak electricity consumption. These secondary effects, related to changes in the composition of total electricity consumption holding  $p$  constant, further influence the choice of how much to spend on total electricity usage.

These two channels are inherent in the properties that the expenditure level objective function inherits from  $W()$ , and it is these properties from which predictions can be drawn regarding total electricity consumption. Standard assumptions regarding these properties

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<sup>5</sup>The aggregated price in our empirical setting will also include a small adjustment for a fixed monthly charge and for the increasing-block structure of the non-TOU rate. This will be discussed in more detail in the following section.

are that  $X$  is a normal good (i.e. within the first channel, the income effect is positive) and that the ancillary substitution effects are relatively small in magnitude (i.e. the second channel, regardless of the direction of its influence, is dominated by the first). Under these conditions, the model predicts that a drop in  $p$  will lead unambiguously to an increase in the quantity demanded of  $X$ .

We use this theoretical framework and its predictions on total electricity consumption as a backdrop when discussing the structure of electricity rates faced by the households in our dataset in the following section, and when discussing our empirical results in the interpretation section below. Of course, the model is also capable of generating predictions concerning load shifting, i.e. the substitution of electricity usage across on-peak and off-peak times. However, we do not discuss these predictions, as our dataset, which we will introduce in Section 4 below, does not provide us with the means to investigate them empirically.

### 3 Program Design

Beginning in 2006, an electricity distribution company in the northeastern United States implemented a mandatory time-of-use (TOU) program for residential customers with high electricity use. Prior to the introduction of this program, most residential customers were billed according to a seasonal flat rate, with the price of electricity varying seasonally but remaining constant within a day. Approximately 12% of customers chose to be placed instead on a seasonal TOU rate, with the price of electricity varying seasonally and within a day. In the analysis that follows, we exclude these voluntary adopters.

Under the policy, when a residential customer's electricity usage in any 30-day billing period exceeded a pre-determined threshold, the customer was automatically placed onto TOU pricing. Beginning November 2006, a household was to be placed on TOU pricing by January of 2008 if usage in any 30-day billing period exceeded 4000 kWh. This threshold

applied until December 31, 2007. The threshold was lowered to 3000 kWh in 2008 and to 2000 kWh in 2009. The present study focuses on households that crossed the 4000 kWh threshold due to the unusual rate change that occurred at that time.

The residential TOU rate plan charges a high per-kWh rate at on-peak times (noon through 8pm on weekdays) and a low per-kWh rate at off-peak times (all other times and days). Table 1 shows the TOU rates that were in effect over the period of our analysis, and compares them to the corresponding non-TOU rates. In our study, the summer non-TOU tariff had an increasing-block structure, with the first 500 kWh of usage in a billing month charged at a base “headblock” per-kWh rate and the remaining usage in that billing month charged at a higher “tailblock” per-kWh rate.

Given this increasing-block structure for the flat rate and the fact that all of the households in our analysis exceed 500 kWh in total electricity consumption in every month, the non-TOU monthly budget constraint can be expressed as

$$p^t(X - 500) + p^h500 + g = E, \quad (4)$$

where  $E$  is total electricity expenditure,  $p^t$  is the tailblock rate,  $p^h$  is the headblock rate, and  $g$  is a fixed monthly charge. Noting once again that total electricity consumption is simply the sum of on-peak and off-peak consumption, this can be re-written as

$$p^t x^{on} + p^t x^{off} - (p^t - p^h)500 + g = E, \quad (5)$$

which emphasizes the fact that the marginal rate faced by non-TOU customers in *both* on-peak and off-peak hours is the tailblock rate. Meanwhile, the TOU monthly budget constraint is given by

$$p^{on} x^{on} + p^{off} x^{off} + g = E, \quad (6)$$

where the fixed monthly charge  $g$  is the same as that for non-TOU customers in all months.

Within the theoretical framework presented in the previous section, total electricity expenditure is defined as the product of the aggregated electricity price and total electricity consumption, or  $E \equiv pX$ . Inserting this definition into equations (5) and (6) and dividing by total consumption gives expressions for the overall non-TOU and TOU electricity prices,

$$p_N = p^t + \phi_N \tag{7}$$

and

$$p_T = sp^{on} + (1 - s)p^{off} + \phi_T, \tag{8}$$

where the subscript  $r \in \{N, T\}$  refers to the non-TOU or TOU regime respectively, and the  $\phi_r$  are small constants based on the fixed charge and the headblock adjustment.

We can now link the rates in Table 1 – and thus the change in the overall electricity price experienced by a household that was switched from the flat rate to the TOU rate – to predictions generated by the theoretical framework. Setting  $\phi_T = \phi_N$  as a convenient approximation for now, it is clear that  $p_T < p_N$  if  $p^t > p^{on} > p^{off}$ , which was the case with the unbundled rates in Table 1 throughout the summer of 2008.<sup>6</sup> Further,  $p_T < p_N$  as well if  $p^{on} > p^t > p^{off}$  and  $s$  is sufficiently small. Therefore, as a first approximation, Table 1 indicates that households that were switched to TOU in 2008 experienced a decrease in the aggregated price of electricity that they faced compared to households that remained on the flat rate. If these households were motivated solely by static price incentives, we would hence

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<sup>6</sup>The unbundled rates include delivery and distribution charges only. They reflect the on-peak/off-peak gradient faced by all customers that chose to pay the generation rates of alternate suppliers, though the absolute level of the all-inclusive rates depends on the specific alternate supplier that a given household was served by, which we do not observe. The bundled rates are the all-inclusive rates that were faced by all customers that chose the EDC as their supplier, which includes about 45% of the EDC's overall customer base. All customers had the EDC in question as distributor, as there are no alternative distributors in the region.

expect, based on the discussion in the previous section and under standard assumptions, that they would have responded by increasing their total electricity consumption. In the interpretation section below, we will demonstrate more formally that these households did indeed face a lower electricity price, but that their response – a decrease in total electricity consumption – cannot be reconciled with a pure static price response.<sup>7</sup>

## 4 Experimental Setting and Data

In this section we explain in detail how the TOU program we study gives rise to a regression discontinuity design, and discuss some nuances of our empirical setting. We then describe the billing data used to identify the effect of mandatory TOU pricing on total usage and total bills.

The key feature of the regression discontinuity design in general is that assignment to the treatment group is triggered by crossing some threshold. In our setting, this occurs when monthly usage exceeds a pre-determined level. For estimated treatment effects to be valid, it must be the case that within the neighborhood of this threshold, assignment to TOU is effectively random. This will occur if some idiosyncratic factors push some individuals over the threshold but not others, or as described by Lee and Lemieux (2010), households lack precise control over the “forcing variable”. We define the forcing variable in our context, according to the rules of the program design discussed above, to be maximum monthly electricity usage between November 2006 and December 2007 net of the 4000 kWh threshold. We will define and discuss this forcing variable more formally in the following section when presenting our empirical specifications.

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<sup>7</sup>The summer of 2008 is the only period in which households faced such a clear price reduction when being switched to TOU. By 2009, the EDC had a more standard TOU pricing scheme, with the on-peak and off-peak rates straddling the non-TOU flat rate. The change in the aggregate price of electricity for households switched to TOU by virtue of crossing either the 3000 kWh or 2000 kWh threshold in more recent years therefore cannot be determined as unequivocally as it can in the present case.

It seems reasonable to assume that households have only imprecise control over their exact electricity usage in any billing period, since precise control would likely require sophisticated equipment for monitoring and regulating usage. The validity of this assumption can be assessed more formally by examining the distribution of the forcing variable. If there were “bunching” in the density of this variable just below the crossing threshold, this might indicate that households could manipulate usage to avoid crossing the TOU threshold. Figure 1 demonstrates that there is no such bunching in our setting, and thus provides supporting evidence that crossing the threshold is random. We will therefore proceed to interpret differences in outcomes between individuals on either side of the threshold as causal effects.

However, one feature of the program – the varying lag across households between crossing a threshold and receiving the TOU treatment – complicates the regression discontinuity design, and in turn affects how the magnitude of these causal effects can be interpreted. To frame the issue, we divide the time period of our analysis into three sub-periods: the pre-experiment period; the qualification period; and the treatment period. The pre-experiment period is defined as the set of months preceding the introduction of the mandatory TOU rule. The qualification period is defined as November 2006 through December 2007, the months during which a household, should it exceed 4000 kWh, would eventually be assigned to TOU pricing. No household was actually assigned to TOU pricing until February 2008.<sup>8</sup> Thus, up until this month there is no difference between crossers and non-crossers in the propensity to be treated. However, not all qualifying households were switched at this point, and indeed, some were not switched for several more months.<sup>9</sup> Therefore, the propensity to be treated

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<sup>8</sup>There were some households that had previously adopted TOU on a voluntary basis, but again, voluntary adopters have been excluded from the analysis. This was done because such self-selection into treatment would invalidate the experimental design.

<sup>9</sup>The long delays between crossing and switching, and the failure to switch some qualifying households altogether, occurred because of technical and administrative difficulties associated with installing requisite metering equipment. Households suffering from a serious illness or other life threatening situation necessitating the use of specialized electrical devices could apply for exemption from the program. We observe a small number of crossers that were switched to TOU but eventually allowed to revert to the non-TOU rate, and interpret this to be the result of the granting of a medical exemption. These households have been

did not immediately jump to 100% in February 2008. The treatment period, the focus of our analysis, comprises June - September 2008, months when most households that crossed the threshold (“crossers”) should have been switched onto TOU. We choose these months to be the treatment period because households on TOU faced an unambiguously lower per kWh rate (net generation) than households on the non-TOU rate during this period.

Another nuance in our setting is that customers would also qualify to be switched to TOU if they breached a lower (3000 kWh) threshold in any month in 2008. This implies that it is possible for some households who never crossed the 4000 kWh threshold to nonetheless be on TOU in the later months of 2008. The joint effect of these two features is that the propensity to be treated increases over time for *both* groups, and thus that the difference in this propensity across groups will be substantial for a limited window only. The fact that “control” households may become treated in greater numbers in the later months of 2008 is another reason that we terminate the treatment period after September 2008.

It follows that, unlike in a canonical “sharp” regression discontinuity setting, in our setting crossing the TOU usage threshold is not a perfect determinant of being in the treatment group in any given month. Instead, the empirical setting should be viewed as having been generated by the Fuzzy Regression Discontinuity (FRD) design, where the “fuzziness” refers to the imperfection of the crosser/non-crosser distinction as a predictor of TOU status in a given treatment-period month. While the FRD design allows us to interpret differences in outcomes between crossers and non-crossers as causal treatment effects, we must adjust their magnitudes for the propensity for each group to be treated. These treatment effects can be estimated consistently only for treatment months in which a sufficiently high proportion of crossers is on TOU relative to the proportion of non-crossers on TOU.

Before turning to a more precise discussion of how we implement the estimation of these

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removed from the analysis. It is possible that some of the crossers that were never switched to TOU were granted a medical exemption pre-emptively, but we cannot observe this.

treatment effects, we describe the billing data and present summary statistics. Monthly billing data beginning in June 2006 on total usage, total expenditure (net of generation) and rate class were provided for a sample of about 35,000 households.<sup>10</sup> Table 2 presents descriptive results at the preferred bandwidth of 600 kWh.<sup>11</sup> The experiment consists of 1,096 households, 34% of which crossed the 4000 kWh threshold at some point in the qualification period. Mean usage and net-of-generation expenditure for this sample amount to 3,309 kWh and \$382 in July 2007, though within this bandwidth there is substantial variation in both usage and expenditure.<sup>12</sup>

## 5 Treatment Effects for Total Usage and Total Bills

### 5.1 Methods

We compare crossers to non-crossers along several dimensions, separately for each month in the entire sample. Specifically, we estimate

$$Y_i = \beta_0^{Yt} + \beta_1^{Yt} C_i + \beta_2^{Yt} f(\tilde{X}_i) + \beta_3^{Yt} C_i \times f(\tilde{X}_i) + \varepsilon_i^{Yt} \quad (9)$$

individually for each month ( $t$ ) and for various dependent variables  $Y$ . The variable  $C_i$  is a dummy variable indicating whether household  $i$  is a crosser. The variable  $\tilde{X}_i$  is the “forcing variable” that determines whether household  $i$  is a crosser. More precisely,  $\tilde{X}_i$  is household

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<sup>10</sup>The dataset is comprised of the population of households with usage above 1500 kWh in September 2010. The year 2010 was chosen so that the included households would be most representative of the EDC’s current customer base. September was chosen because it corresponded to the annual system peak that year.

<sup>11</sup>Bandwidth will be discussed in the following section and in Section A.1.

<sup>12</sup>Table 2 does not report descriptive statistics on peak and off-peak usage because we do not have data on these variables. As we are relying on billing data, and since utilities have no need to meter usage by time of day if they do not charge time-varying rates, our dataset does not include information on the on-peak/off-peak breakdown of total usage for non-TOU household-months. As discussed in the interpretation section below, this breakdown can be inferred from billing data and rates for TOU household-months. However, without information for non-TOU household-months, we are unable to assess the effect of the switch to TOU on this breakdown.

$i$ 's maximum total usage across all billing periods during the qualification period net of the kWh threshold. Under the rules of the program, if  $\tilde{X}_i$  is strictly greater than zero, household  $i$  is a crosser and should receive the TOU treatment eventually.<sup>13</sup>

The dependent variables we consider are total usage, total bills, and a dummy variable  $TOU_{it}$  indicating whether household  $i$  was on TOU pricing (i.e. was treated) in month  $t$ . Specification (9) allows for a flexible relation between the outcome variable of interest and the forcing variable through the function  $f(\cdot)$ , and allows this relation to differ for crossers and non-crossers.<sup>14</sup> The parameter  $\beta_1^{Yt}$  measures the effect of being a crosser on the level of outcome variable  $Y$  in month  $t$  as the distance from the threshold approaches zero, and is interpreted as the Intent to Treat effect (ITT). These are causal effects by virtue of our assumption – discussed and supported in the previous section – that, as the distance from the threshold approaches zero, a household's crossing status is exogenous.

The fuzzy regression discontinuity treatment effect for outcome  $Y$  in any month  $t$  in the treatment period is defined as

$$\tau_{FRD}^{Yt} \equiv \frac{\beta_1^{Yt}}{\beta_1^{TOUt}}. \quad (10)$$

That is, the treatment effect for the outcome of interest is the ratio of the ITT for the outcome of interest to the ITT for the propensity to be treated.<sup>15</sup> It can be estimated

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<sup>13</sup>Formally, let  $X_{it}$  be household  $i$ 's total electricity usage in month  $t$ . Further, let usage on a standardized 30-day-billing-period basis be  $\ddot{X}_{it} \equiv X_{it}/d_{it} \times 30$ , where  $d_{it}$  is the number of total days actually in the billing period corresponding to household  $i$ 's bill in month  $t$ . Then  $\tilde{X}_i \equiv \left( \max_{t \in \mathbb{Q}} \{ \ddot{X}_{it} \} - \bar{X} \right)$ , where  $\mathbb{Q}$  is the set of months in the qualification period and  $\bar{X}$  is the threshold; and  $C_i \equiv \mathbb{1} \{ \tilde{X}_i > 0 \}$ , where  $\mathbb{1} \{ \cdot \}$  is the indicator function. The households included in these regressions are only those with a value of the forcing variable  $\tilde{X}_i$  within a selected bandwidth around zero, i.e. households “close to” the threshold. As discussed below, we first use a wide bandwidth to visually examine the data and then use an optimal bandwidth to estimate treatment effects.

<sup>14</sup>We first define  $f(\cdot)$  as a fourth-order polynomial to visually examine the data, then as linear to estimate the treatment effects. Within the optimal bandwidth, we do not find alternatives to the linear form to qualitatively affect our estimated treatment effects.

<sup>15</sup>See Lee and Lemieux (2010), p. 300 for a discussion of how the FRD treatment effect thus defined is equivalent, under the standard local average treatment effect assumptions, to the average treatment effect

by applying two-stage least squares to the following system of equations for any outcome variable  $Y$  in a given treatment-period month  $t$ :

$$Y_i = \tau_0^{Yt} + \tau_1^{Yt} TOU_i + \tau_2^{Yt} f(\tilde{X}_i) + \tau_3^{Yt} C_i \times f(\tilde{X}_i) + \omega_i^{Yt} \quad (11)$$

$$TOU_i = \beta_0^{TOUt} + \beta_1^{TOUt} C_i + \beta_2^{TOUt} f(\tilde{X}_i) + \beta_3^{TOUt} C_i \times f(\tilde{X}_i) + \varepsilon_i^{TOUt}, \quad (12)$$

where  $\hat{\tau}_{1,2SLS}$  is numerically equivalent to inserting the ITTs estimated via specification (9) into equation (10).

## 5.2 Preliminary Evidence

We begin by visually examining the propensity to be treated, total billed amount, and total usage on each side of the threshold in July 2008. Specifically, we estimate specification (9), including households within a very wide range around the threshold and allowing the relation between the outcome variable and the forcing variable to have a separate quartic form on each side of the threshold. This provides a first look at whether the relation exhibits a discontinuity at the threshold (i.e. an intent to treat effect), and allows us to diagnose any non-linearities that may complicate the identification of a discontinuity.

Figure 2 shows the estimated propensity to receive the TOU treatment for crossers (households that exceeded the 4000 kWh threshold) and non-crossers. Crossing the threshold is clearly a strong predictor of having received the TOU treatment by July 2008, as illustrated by the dramatic discontinuity at the threshold. However, it is not a perfect indicator, as some non-crossers just to the left of the threshold – i.e. whose maximum 30-day usage during the 4000 kWh qualification period was very close but did not exceed the 4000 kWh threshold – have a small but positive propensity to be treated. Likewise, a few crossers still had not

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for compliers in a potential outcomes framework.

received the TOU treatment by July 2008.

In Figures 3 and 4, we present the estimated total billed amount and usage, respectively, on each side of the 4000 kWh threshold in July 2008. These graphs illustrate a discontinuity both in expenditure and usage at the threshold, suggesting that a crosser had a substantially lower electricity bill than a non-crosser at the threshold (by about \$100). While the relation in Figure 3 exhibits some non-linearity, particularly for very high levels of the forcing variable, these figures provide fairly clear evidence that the difference in usage and expenditure is indeed the result of a discontinuity.

### 5.3 Treatment Effects

Having provided visual evidence of the discontinuity, we now restrict specification (9) to be linear in the forcing variable and in its interaction with crossing status, and include only households within a narrower, optimally-chosen bandwidth of 600 kWh.<sup>16</sup> We use this form to identify ITTs for each dependent variable for several pre-qualification and qualification months, as well as our treatment months of June - September 2008. To present the results as compactly as possible, we graph time series of the set of estimated coefficients for each of the three dependent variables. For dependent variable  $Y$ , we graph  $\hat{\beta}_0^{Yt}$  – the estimate of outcome  $Y$  in month  $t$  for a non-crosser exactly at the threshold – and  $\hat{\beta}_0^{Yt} + \hat{\beta}_1^{Yt}$  – the same for a crosser exactly at the threshold – for every month, also indicating when the difference between the two is statistically significant.

Figure 5 graphs the ITT of the probability that a crosser receives the TOU treatment for each individual month between June 2006 and January 2009.<sup>17</sup> The months between the

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<sup>16</sup>The method used to determine the optimal bandwidth is described in Section A.1. A larger bandwidth leads to more precise estimates of the discontinuity. However, it also means that households further away from the threshold are being used to identify the discontinuity *at* the threshold, which can impart a bias.

<sup>17</sup>The bandwidth is symmetric, so encompasses households with a value of the forcing variable between -600 kWh and 600 kWh. Note that the data in Figure 2 have been smoothed for ease of presentation, so that each point represents several households. The point for July 2008 in Figure 5 is based on straight lines of best fit through the first 7-8 points on each side of the threshold in Figure 2.

vertical lines delineate the qualification period, and the months further to the left are the pre-experiment period. This figure illustrates that crossing the TOU threshold is a strong predictor of TOU pricing in the treatment period. In the pre-experiment and qualification periods the propensity to be on time-of-use pricing is zero for both crossers and non-crossers by construction, since we restrict our sample to households that did not receive the treatment during the qualification period.<sup>18</sup> However, by October 2008, the proportion of control households that had been switched to TOU by virtue of crossing the 3000 kWh threshold earlier that year was so high that treatment effects cannot be consistently estimated for this month onwards.

We present the estimated ITTs on the total bill in Figure 6. The large discontinuity illustrated in Figure 3 for July 2008 is also present for the other treatment months, with 95 percent confidence. We also observe that the estimated total bill was nearly identical for crossers and non-crossers throughout the pre-experiment and qualification periods. This balance on pre-determined observables is consistent with the intent to treat being randomly assigned at the threshold. It also suggests that the large ITTs observed in the summer 2008 are not spuriously caused by systematic difference in summer usage patterns between crossers and non-crossers.

Figure 7 illustrates the estimated ITTs on total electricity usage over time. Total usage was nearly identical between crossers and non-crossers throughout the pre-experiment and qualification periods, providing evidence of another observable along which the two groups are balanced. However, during the treatment periods, there is a significant difference in total usage in June and July 2008, when crossers at the threshold exhibited lower usage than non-

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<sup>18</sup>Households with a value of the forcing variable substantially higher than the upper bandwidth cut-off of 600 kWh are more likely to have crossed the 4000 kWh threshold for the first time early in 2007, and such households were required to have been switched to TOU before the end of 2007. A few of these households were indeed switched in late 2007, but most were not switched until February 2008. The delay in rolling out the program for these larger households (which are not included within the bandwidth we consider in any case) appears to be due to unforeseen technical and administrative issues faced by the EDC.

crossers at the threshold. We also see some visual evidence of lower usage for TOU households in August and September, though we cannot distinguish these from zero with confidence. The absence of significant differences in total usage between crossers and non-crossers during the pre-experiment and qualification periods indicates that the differences in June and July 2008 are not driven by pre-existing differences between the groups. It also indicates that non-crossers were not purposely restraining their usage during the qualification period to avoid crossing the threshold, which would violate the random assignment assumption.

Table 3 shows the treatment effects, adjusted for the propensity to be treated, on total usage and total bills for each month in the treatment period. To give a better sense of magnitudes, treatment effects are reported as a percentage of the level of the respective variable for non-TOU households at the threshold.<sup>19</sup> We find that the switch to TOU pricing caused economically and statistically significant reductions in electricity expenditure in all treatment months, of at least 21% and as much as 30% in July. This is matched by statistically significant declines in total electricity usage in June and July of 9-10%, and noisy declines of 5 and 2 percent in August and September, respectively.

When interpreting the expenditure estimates, it seems natural that electricity expenditure would decline or remain unchanged since customers on TOU faced lower peak and off-peak rates compared to flat rate households. In contrast, basic intuition suggests that demand for electricity should increase with a reduction in electricity prices; yet we find the opposite to be true. We now investigate the revealed choice behavior more directly.

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<sup>19</sup>That is, each entry shows  $\hat{\tau}_1^{Y^t}/\hat{\tau}_0^{Y^t} \times 100$  from a separate two-stage least squares application of equations (11)-(12). We discuss the bootstrap methods we employ to estimate the standard errors of these transformed coefficient estimates in Section A.2

## 6 Interpretation

To assist us in digesting the empirical results, we turn to Figures 8 and 9, which provide a simple visual way to evaluate the nature of consumer choice. These figures present graphs of budget frontiers and revealed choices as implied by the empirical results described in Table 3. Each graph presents the consumption bundle chosen by TOU customers, as well as two budget frontiers. These features of the choice setting are derived directly from prices and estimates of behavior in treatment (TOU) and control (non-TOU) *at the threshold*. The TOU consumption bundle is revealed arithmetically from the relationship between total consumption ( $\hat{\tau}_0^{kWh_t} + \hat{\tau}_1^{kWh_t}$ ) and the TOU tariff rates. Budget frontiers are determined by the revealed expenditure level at the threshold (also from the application of the 2SLS estimation) and relative prices.<sup>20</sup>

The first frontier is based on non-TOU rates and the level of expenditure of the non-TOU household, and has a slope of -1 to reflect equality of peak and off-peak prices. This frontier represents all combinations of on-peak and off-peak usage that sum to the estimated non-TOU total usage at the threshold. Note that any point on the interior of this frontier is unequivocally a drop in total consumption relative to the non-TOU bundle. The second, analogous, frontier is based on TOU rates and the expenditure of the non-TOU household at the threshold. Were expenditure for treated households to remain at the revealed non-TOU level, this second frontier represents the upper limit of the feasible set of TOU bundles. Each budget constraint is presented separately for the months June to September 2008.

We present two different rate types – unbundled in Figure 8 and bundled in Figure 9 – to reflect differences in the TOU gradient between two customer types in our sample. Unbundled rates are paid by customers who have elected to purchase electricity generation

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<sup>20</sup>Algebraically, the budget frontiers are expressed by equations (5) and (6), with the values of actual rates and revealed total expenditure inserted where appropriate. The imputation of the TOU consumption bundle is discussed in Section A.3. A technical issue involving an adjustment of calendar-month rates for billing cycles that is necessary for implementing this imputation is discussed in Section A.4.

from an “alternate supplier” (i.e. not from the regulated electricity distribution company). During the period of analysis, all alternate supplier generation rates were time-invariant,<sup>21</sup> implying that the entire TOU gradient was transmitted through the unbundled price for these customers. On the other hand, bundled rates include generation charges that are paid to the electricity distribution company. In our setting, these generation charges transmit an additional peak/off-peak price gradient. As such, the choice setting is different for customers who have elected to purchase generation from an alternate supplier than for those purchasing exclusively from the regulated utility, so we present budget frontiers separately for each.

Recall that the TOU rates/non-TOU expenditure frontier represents the theoretical maximum consumption possibilities available to a household that is switched to TOU pricing and retains the non-TOU level of electricity expenditure. This line describes the frontier of the feasible set of on-peak/off-peak bundles from which a treated household could choose if on-peak and off-peak electricity were the only two goods consumed. The bundle chosen by the control household at the threshold lies somewhere on the non-TOU rates/non-TOU expenditure line, and from these figures it is therefore apparent that the chosen TOU bundle was feasible under the non-TOU budget and rates. Thus the original non-TOU bundle is revealed preferred to the TOU bundle. Note that this is true irrespective of the presence of crossing of the budget constraints (which we discuss below). In this simplified two-good representation, each graph illustrates an outcome in which treated consumer choices violate the Weak Axiom of Revealed Preference (WARP).

A more realistic interpretation of the setting includes an outside consumption good in addition to both electricity goods, as in the theoretical framework presented in the second section. When we allow for the presence of an outside good, changes in electricity rates will affect how much of this outside good is purchased, and thus how much of the household’s

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<sup>21</sup>A thorough search of alternate supplier rates by the authors in 2010 confirmed what our utility partners asserted: time-varying generation rates were not offered by alternate suppliers until more recently.

(unobserved) monthly income is allotted for total electricity consumption. Specifically, when the TOU bundle is interior to the TOU rates/non-TOU expenditure line, it is associated with lower total electricity expenditure, and thus an increase in the quantity of the outside good consumed by the TOU household at the threshold compared to the non-TOU household at the threshold. Here we will distinguish between regions in which the TOU rates/non-TOU expenditure frontier lies above the non-TOU frontier, and those in which it lies below.

In regions where the TOU rates/non-TOU expenditure constraint is on the exterior of the non-TOU constraint, the outside good has become relatively more expensive in treatment (i.e. the overall price of electricity has fallen while the absolute price of the composite non-electricity good is assumed to be the same for the non-TOU and TOU households at the threshold). In these cases, if the reduction in total electricity consumption that we observe and the increase in consumption of the outside alternative that this implies were to be consistent with static price incentives, one of two abnormal conditions would have to hold: either the outside good would have to be associated with substantially stronger substitution patterns with peak or off-peak consumption individually than with total electricity consumption overall;<sup>22</sup> or total electricity consumption would have to be associated with a negative income elasticity so large as to make electricity a Giffen good. We consider these to be unsatisfactory explanations with which to reconcile the empirical findings.

In regions where the TOU rates/non-TOU expenditure frontier is interior to the non-TOU budget (i.e. in the lower-right region of the graphs where the frontiers cross), the story becomes slightly more nuanced. For households consuming in that region, the switch from the flat rate to TOU implies an increase in the overall price of electricity. In this case, a net decrease in electricity consumption can be explained by static price incentives under

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<sup>22</sup>For example, if off-peak consumption were strongly complementary with non-electricity consumption, the drop in the off-peak rate could induce such a large increase in consumption of the outside good that the share of income remaining for electricity consumption might be reduced enough that total electricity consumption would have to decrease.

standard assumptions. However, the likelihood of any household’s chosen peak/off-peak bundle residing in this region is essentially zero. In months where we observe a cross in the budget frontier, this crossing occurs at an extremely high peak/off-peak ratio. Appealing to an external dataset on the peak-to-off-peak usage ratio for a random sample of customers, we can examine the likelihood that the observed “crossing” ratio falls within the observed range of ratios.<sup>23</sup> With the exception of bundled rates for June, the crossing ratio is much higher than any peak-to-off-peak ratio observed in the data. Even for a customer on a bundled rate in June, the “crossing” ratio is in the 99th percentile of the observed distribution. We hence consider extreme preferences for on-peak electricity usage to be an unlikely explanation for our results.

The abundance of evidence does not allow much scope to conclude that household choice behavior is being driven solely by static price incentives. A two-good view leads immediately to violations of WARP. When we allow for the consumption of an outside good, either extreme assumptions regarding income or cross-price elasticities must be made, or the intensity of peak electricity use must be assumed to be of a degree inconsistent with observed data.

So where does this leave us? One might conjure several reasonable explanations to rationalize the observed behavior. While we are not able and thus do not strive to test them here, we consider this an important area of future research. We hope that a description of some of these hypotheses will be helpful to readers.

One hypothesis allows for a consumer who is motivated by dynamic as well as static price incentives. In our setting, the peak price did eventually increase. A consumer correctly expecting this increase in future rates ought to incorporate such expectations into the choice of durable goods investments.<sup>24</sup> That is, if electricity is expected to become more expensive

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<sup>23</sup>This load profile dataset comprises hourly usage data between January 2006 and October 2011 for a random sample of households present for between 2 and 48 months. Figure 10 shows the peak-to-off-peak usage ratio by total usage for selected summer months from this dataset.

<sup>24</sup>See Rapson (2013).

during peak hours of air conditioning demand in the future, a rational, forward-looking consumer may be willing to pay for a more energy-efficient air conditioner *today*. Making such a choice would manifest in lower derived electricity demand for electricity today, which is consistent with behavior in our setting.

Another potential hypothesis that could explain the observed outcome is that households were not only responding to contemporaneous rates, but also engaging in what is becoming known as “intermittent updating.” Under this hypothesis, consumers are attentive to choices infrequently, and thus may exhibit behavior in the present corresponding to incentives that were operative sometime in the past. In our setting, this might imply that households were not responding to the change to the TOU price relative to the corresponding non-TOU price, but rather relative to whatever overall price of electricity they faced the last time they updated their choices. Intermittent updating may equivalently be thought of as a symptom of “rational inattention,” whereby consumers educate themselves about their energy consumption in response to (new) incentives provided by the TOU rate structure.<sup>25</sup>

Finally, there is a growing body of evidence on the importance of “behavioral” considerations in this choice setting. Each treated household received a letter notifying them of their new rate plan, and it is possible that receipt of the letter itself was responsible for the observed treatment effect. There is some evidence from the literature that is consistent with this explanation. For example, households who are informed that their usage is abnormally high tend to engage in behavior that brings them closer to the norm (Allcott (2011)). Since treated households in our setting were told that they had “high” usage when they were informed that they were being switched to TOU due to crossing the threshold, this information may have induced a response towards conforming to social norms, or perhaps even an attempt to atone for or counteract this high usage.

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<sup>25</sup>While we remain agnostic about mechanisms, support for the intermittent updating hypothesis or the broader rational inattention hypothesis resides in the fact that hundreds of households just below the threshold could have saved substantial amounts by volunteering for TOU, but didn’t.

## 7 Conclusion

This study has exploited a natural experiment to document an instance in which households appear to have been motivated by factors beyond static price incentives. Despite growing evidence that non-monetary and inter-temporal factors are important in a wide range of settings, there are few well-identified cases of this behavior in environmental economics. Evaluating customer response to price incentives is a necessary step in achieving a deeper understanding of consumer energy choices and, in turn, designing more effective market-based energy and environmental policies.

The randomized nature of assignment into TOU pricing that arises from the structure and implementation of the program provides us with an experimental setting to evaluate consumer behavior. Customers were automatically placed on the TOU rate after exceeding the usage threshold, creating an appropriate setting in which to apply a regression discontinuity design. Our research design, underpinned by the large-scale deployment of the program, differentiates our work from most studies of time-varying electricity pricing, which usually rely on framed field experiments in which participants are aware of their participation.<sup>26</sup> Thus, our paper offers a novel estimate of how certain residential consumers may behave when exposed to a change in the overall price of electricity such as the one induced by the switch to TOU in our case.

Admittedly, the households in our setting are very large, and not representative of the “average” electricity user. On the other hand, the intensity of electricity use that they exhibit makes them a particularly important target for energy conservation efforts. In any case, we do not consider the value of our work to lie in how well our findings will predict the outcome of any given price intervention. Nor do we feel that our findings should dissuade

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<sup>26</sup>We refer here to the taxonomy of field experiments proposed by Harrison and List (2004). Wolak (2006) and Jessoe and Rapson (forthcoming) are examples of recent studies of the effect of time-varying pricing that are based on framed field experiments.

policymakers from implementing price-based policies in general. Rather, we hope that our results will serve as a simple warning that market-based policies are not well-designed policies just by virtue of being market-based. Price interventions will be most effective when their designs are sufficiently cognizant of the full spectrum of incentives they will impart.

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## Tables and Figures

Table 1: Electricity Rates, 2008, Cents per kWh

	Non-TOU		TOU	
	Headblock	Tailblock	On-Peak	Off-Peak
<b>unbundled</b>				
Jun.	7.9	11.8	11.4	7.6
Jul.	8.6	12.6	12.0	8.1
<b>bundled</b>				
Jun.	20.1	24.1	26.2	18.9
Jul.	20.6	24.6	26.5	19.2

Notes: Unbundled rates include distribution, transmission, and delivery charges plus fees only. Bundled rates also include the generation prices that were charged by the utility to those customers opting to keep the utility as both distributor and supplier. About 55% of the customer base opted to pay generation prices charged by alternate suppliers; no alternate suppliers had TOU generation prices, so the unbundled rates represent the relative on-peak/off-peak all-inclusive rates faced by these customers, but not the absolute levels. The headblock is the first 500 kWh of total usage in the billing month. The July rates stayed in place through September.

Table 2: Summary Statistics

	Total			
	Usage (kWh)	Total Bill (\$)	Crossers (%)	<i>N</i>
July 2007	3,309 [751]	382 [91]	0.339 [0.473]	1,096

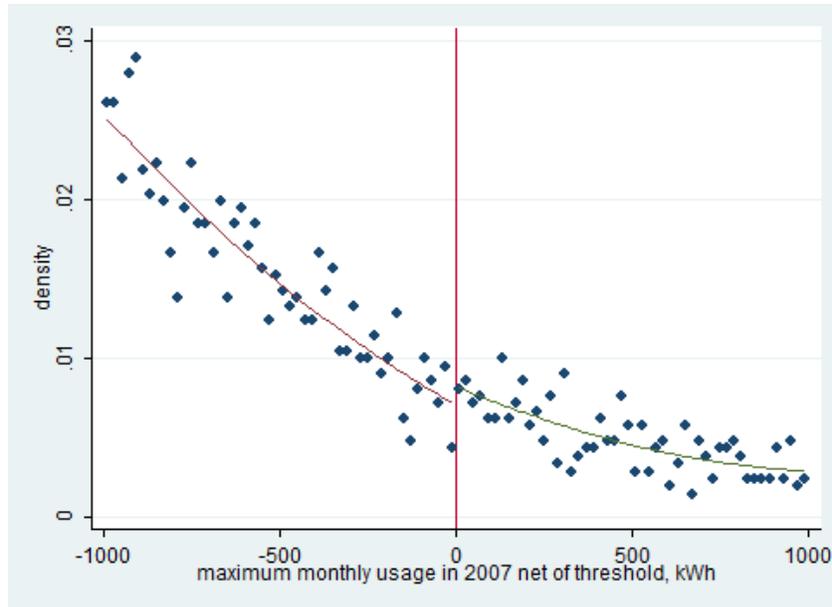
Notes: Standard deviations are in square brackets. The households included are those within the optimally-chosen 600 kWh bandwidth; see the text for details.

Table 3: Treatment Effects (%)

	<b>Total Usage</b>		<b>Total Bill</b>		<i>N</i>
Jun. 2008	-9.24	**	-21.50	***	1,105
	(4.69)		(4.19)		
Jul. 2008	-9.85	***	-30.06	***	1,105
	(3.73)		(2.96)		
Aug. 2008	-5.39		-26.15	***	1,107
	(4.04)		(3.08)		
Sep. 2008	-2.11		-22.31	***	1,095
	(5.82)		(4.36)		

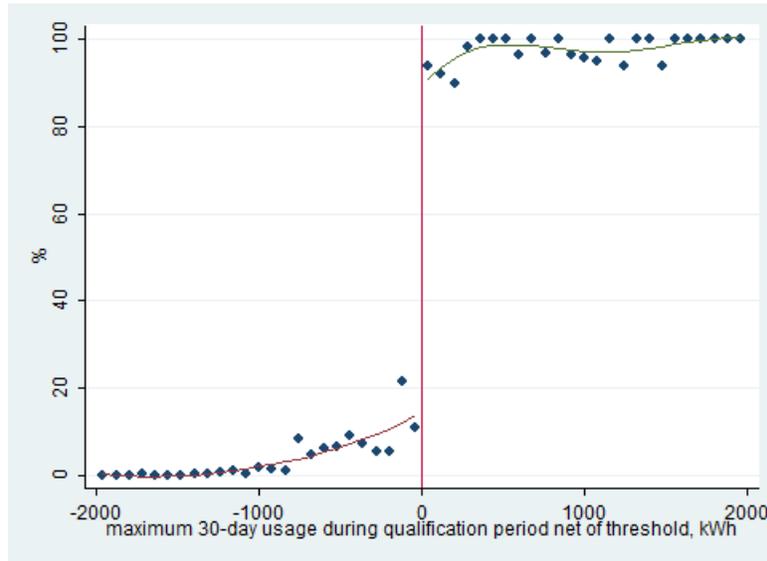
Notes: Standard errors (in parentheses) are based on a non-parametric bootstrap with 1,000 replications. Significance at the 1% (\*\*\*), 5% (\*\*), and 10% (\*) levels is indicated. Each estimate is from a separate regression, and is the estimated TOU treatment effect as a percentage of the estimated non-TOU level at the threshold for the respective dependent variable. Of the 1,105 households included in the regressions for July 2008, 373 are crossers; and the distribution of households is similar in other months. The households included are those within the optimally-chosen 600 kWh bandwidth; see the text for details.

Figure 1: Density of the Forcing/Running Variable



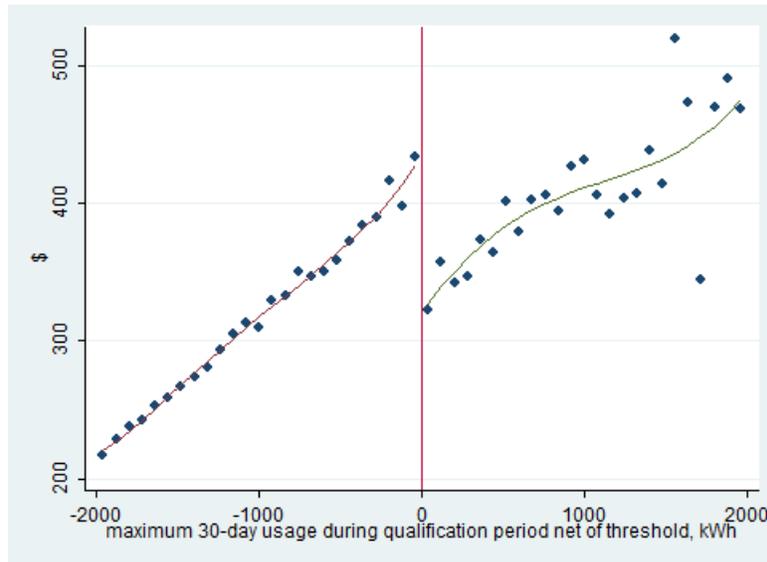
Notes: Data are smoothed into bins of width 20 kWh. Separate quadratic predictions on each side.

Figure 2: Intent to Treat Effect, Propensity to be Treated, July 2008



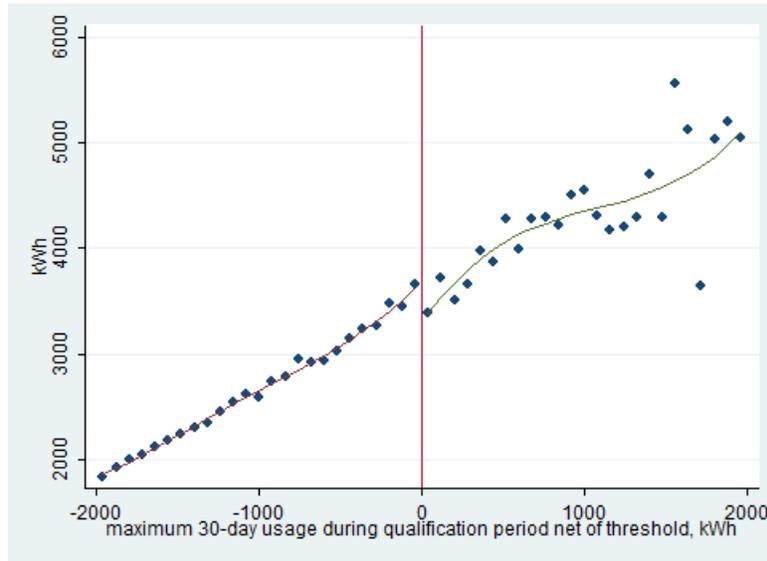
Note: Data are smoothed into bins of width 80 kWh.

Figure 3: Intent to Treat Effect, Total Bill, July 2008



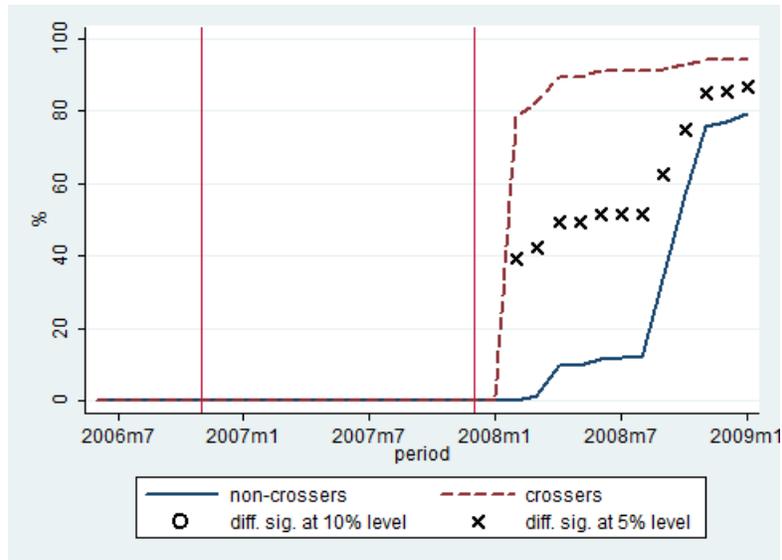
Note: Data are smoothed into bins of width 80 kWh.

Figure 4: Intent to Treat Effect, Total Usage, July 2008



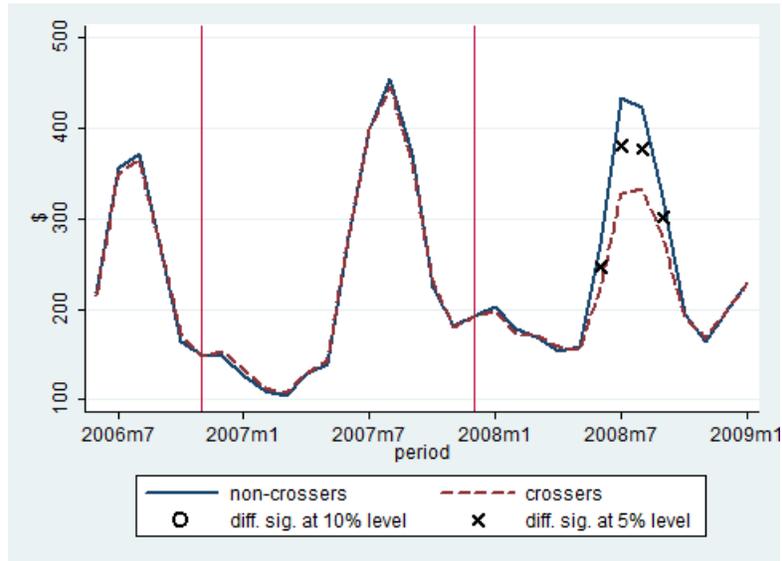
Note: Data are smoothed into bins of width 80 kWh.

Figure 5: Intent to Treat Effects, Propensity to be Treated, All Months



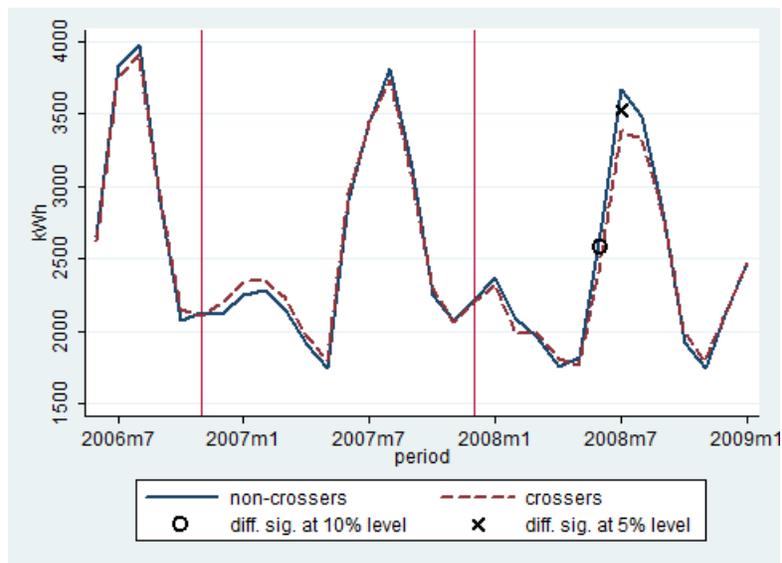
Notes: The qualification period is the set of months between the vertical lines. The households included are those within the optimally-chosen 600 kWh bandwidth; see the text for details.

Figure 6: Intent to Treat Effects, Total Bill, All Months



Notes: The qualification period is the set of months between the vertical lines. The households included are those within the optimally-chosen 600 kWh bandwidth; see the text for details.

Figure 7: Intent to Treat Effects, Total Usage, All Months



Notes: The qualification period is the set of months between the vertical lines. The households included are those within the optimally-chosen 600 kWh bandwidth; see the text for details.

Figure 8: Budget Lines, Unbundled Rates

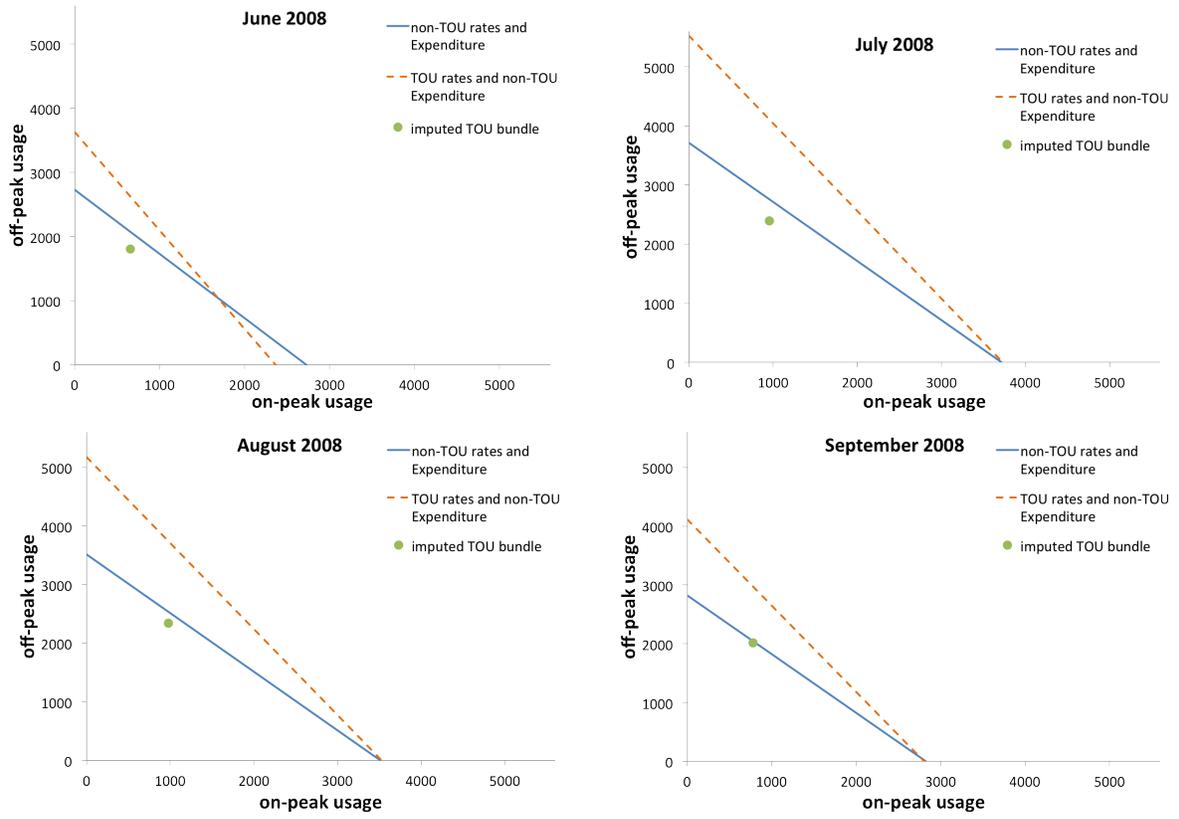


Figure 9: Budget Lines, Bundled Rates

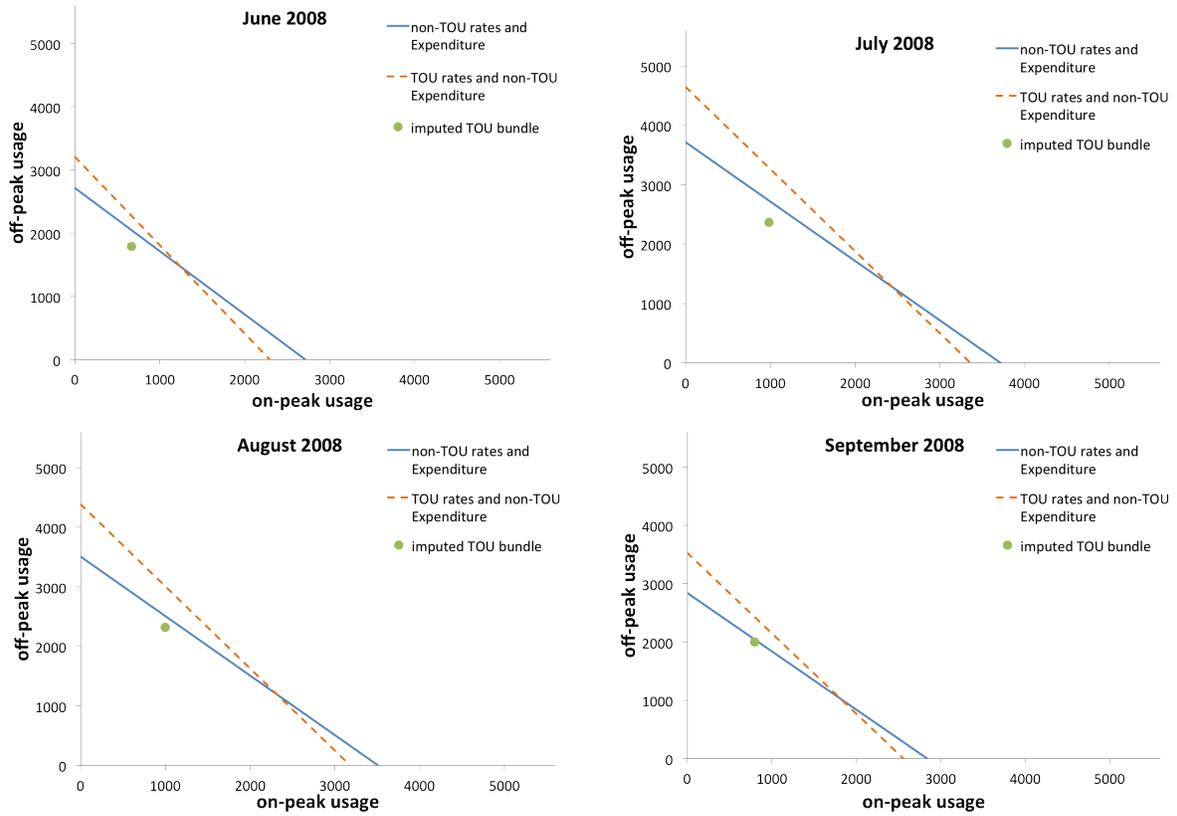


Figure 10: Peak-to-Off-Peak Usage Ratio by Total Usage in the Load Profile Sample, Calendar Month of July, 2006-2011

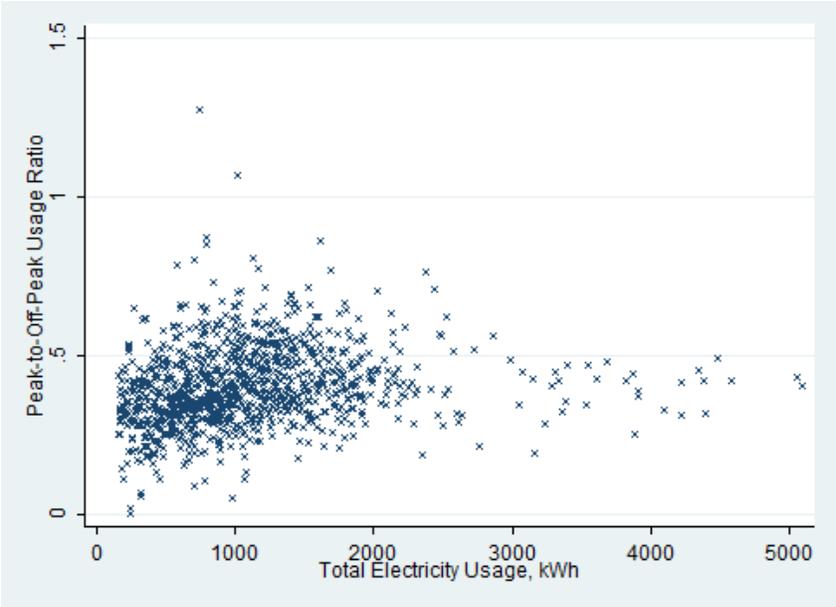


Figure 11: Sensitivity to Bandwidth, Total Usage, July 2008

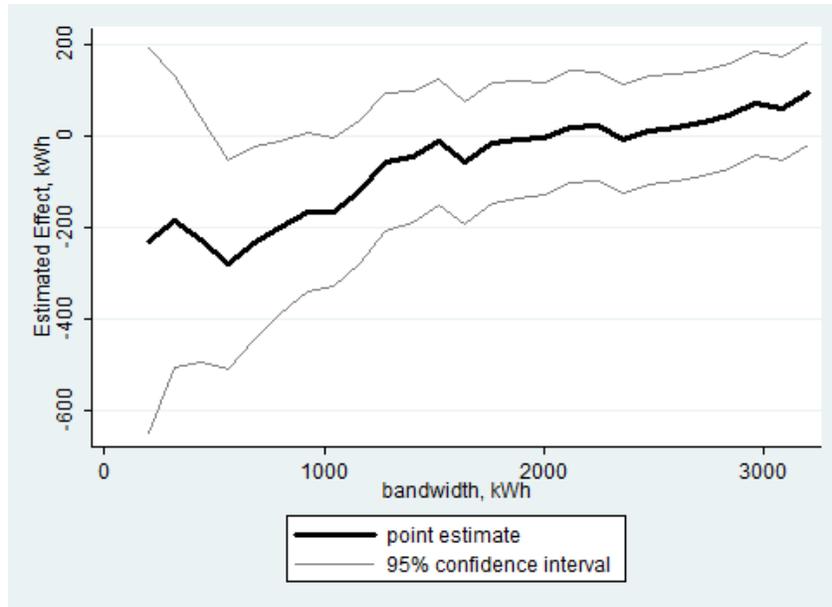
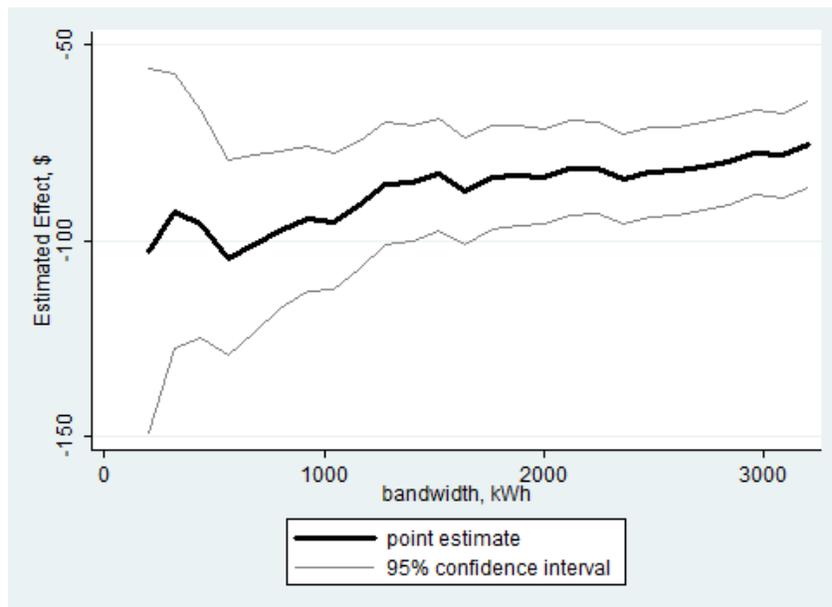


Figure 12: Sensitivity to Bandwidth, Total Bill, July 2008



# A Appendix

## A.1 Bandwidth

The trade-off involved with increasing the bandwidth is as follows: on the positive side, the precision of the estimate is improved; on the negative side, a bias is imparted on the estimate of the effect *at* the threshold by including observations further away from the threshold. As discussed by Lee and Lemieux (2010), when the relationship between the forcing variable and the outcome variable is approximately linear on both sides of the threshold, the bias concern becomes less prominent (and, therefore, the optimal bandwidth exercise less useful).

Lee and Lemieux (2010) suggest a plug-in rule-of-thumb bandwidth that we implement in order to derive the optimal bandwidth used in the text and figures. Imbens and Kalyanaraman (2012) provide a completely data-driven approach to selecting an optimal bandwidth, which we have found to produce similar results. In either case, we wish to adopt a uniform bandwidth for every month, dependent variable, and estimator (ITT or treatment effect). To do so, we apply the two-stage rule-of-thumb procedure with a quartic form common to each side of the threshold repeatedly for various treatment months and the ITT specification with total usage and total expenditure as dependent variables. From the set of optimal bandwidth estimates thus produced, we informally choose one in the lower range to apply uniformly in the estimation of all ITTs and treatment effects.

Figures 11 and 12 show the ITT on total usage and the total bill in July 2008, with 95% confidence bounds, for bandwidths ranging from 200 kWh to 3200 kWh on either side of the threshold. The graphs shows a rapid tightening of the confidence interval and relative stability in the absolute magnitude of the point estimate up to a bandwidth of about 1000 kWh. For both usage and total bill, there is a steady decrease in the absolute magnitude of the point estimate and moderate tightening of the confidence interval beyond the 1000 kWh bandwidth. Correspondingly, as shown in Figures 3 and 4, beyond a value of the forcing

variable of about 1000 kWh to the right of the threshold, the relation with the usage and bill outcome variables becomes quite non-linear, indicating, along with Figures 11 and 12, that bias is becoming a more prominent concern than precision.

## A.2 Bootstrapped Standard Errors

We use nonparametric bootstrap methods to perform statistical inference on the treatment effects for total usage and total bills, which are estimated in levels but reported as percent changes. In this section, we describe the sampling method that we have used. In both notation and procedure, what follows draws upon Cameron and Trivedi (2009).

Let  $w_i$  denote the full time series of data for household  $i$ ,  $w_i = (X_i, E_i, TOU_i, C_i, \tilde{X}_i)$  (corresponding to the notation in equation 9, where  $Y$  referred generically to either total usage ( $X$ ), total expenditure ( $E$ ), or the treatment indicator ( $TOU$ )). We draw a bootstrap sample of size  $N$  by sampling  $w_1, \dots, w_N$  with replacement at the household level from the subsample of the billing dataset corresponding to the optimal bandwidth restriction. Denoting the bootstrap sample by  $w_1^*, \dots, w_N^*$ , we calculate an estimate,  $\hat{\theta}^*$ , of the vector of parameters of interest,  $\theta$ , and apply our desired transformation  $f(\hat{\theta}^*)$  to these parameter estimates. We repeat this for a total of 1000 separate bootstrap samples. Given the 1000 bootstrap estimates,  $f(\hat{\theta}_1^*), \dots, f(\hat{\theta}_{1000}^*)$ , we calculate the bootstrap estimate of the variance-covariance matrix according to

$$\hat{V}_{Boot}(f(\hat{\theta})) = \frac{1}{999} \sum_{b=1}^{1000} \left( f(\hat{\theta}_b^*) - \overline{f(\hat{\theta}^*)} \right) \left( f(\hat{\theta}_b^*) - \overline{f(\hat{\theta}^*)} \right)' \quad (13)$$

where  $\overline{f(\hat{\theta}^*)} = \sum_{b=1}^{1000} f(\hat{\theta}_b^*)/1000$ .

### A.3 Imputation of the TOU Consumption Bundle

We do not observe on-peak and off-peak usage in our billing dataset, but we can use the structure of customers' electric bills to impute a household's on-peak and off-peak usage for months that it is on TOU. When household  $i$  is on TOU, its total billed amount  $E$  in month  $t$  is

$$E_{itT} = p_{tT}^{on} x_{itT}^{on} + p_{tT}^{off} x_{itT}^{off} + g_{tT} \quad (14)$$

where  $T$  indicates the TOU pricing regime and  $x^{on}$  and  $x^{off}$  represent the household's on-peak and off-peak usage respectively. That is, bills depend on a fixed fee  $g$ , and on on-peak and off-peak per-kWh charges of  $p^{on}$  and  $p^{off}$  respectively. Combining this with the fact that on-peak and off-peak usage must sum to the household's observed total usage,  $X$ , i.e.

$$X_{itr} = x_{itr}^{on} + x_{itr}^{off} \quad (15)$$

(for either pricing regime  $r \in \{T, N\}$ ), gives two equations in two unknowns. This allows us to solve for on-peak and off-peak usage as functions only of variables that we observe:

$$x_{itT}^{on} = \frac{E_{itT} - g_{tT} - p_{tT}^{off} X_{itT}}{p_{tT}^{on} - p_{tT}^{off}} \quad \text{and} \quad x_{itT}^{off} = \frac{p_{tT}^{on} X_{itT} - g_{tT} - E_{itT}}{p_{tT}^{on} - p_{tT}^{off}}. \quad (16)$$

For the TOU household *at the threshold*, the 2SLS coefficient estimates are inserted as appropriate into these expressions. The corresponding rates must be adjusted to ensure that they reflect the billing cycle that this threshold TOU household is on, which is accomplished as described in the following section.

Note that this imputation is, unfortunately, impossible for non-TOU household-months, as the non-TOU rate is the same for on-peak and off-peak usage, and the non-TOU analogues to the expressions in (16) are hence undefined.

## A.4 Billing Cycles

There were 17 distinct billing cycles for residential customers over the period covered by our dataset. Each billing cycle corresponds to a given day of the month (which can change by a couple of days in either direction depending on month and year, due to weekends and holidays) on which the meter is read and the billing period for customers on that billing cycle closes. For customers on billing cycle 1, the total usage and total bill data for “July 2008”, for example, correspond to usage that mostly happened in the calendar month of June; on the other hand, for customers on billing cycle 17, total usage and total bill data for “July 2008” correspond to usage that mostly happened in the calendar month of July. There is thus heterogeneity in our billing data in what “July 2008” (and every other month) refers to. This is relevant because we only have rate information on a calendar-month basis. So the total bill in “July 2008” depends on a weighted average of the rates that were in place in the calendar month of June and those that were in place in the calendar month of July, with the appropriate weight depending on which billing cycle a household is on. We describe here how we retrieve billing cycle weights by household-month, and how we apply the weights thus retrieved to align variables observed on a calendar-month basis with variables observed on a billing-month basis.

We reconstruct the total billed amount for all non-TOU household months based on the observed unbundled rates, total usage, and the unknown weight; then solve for the weight that exactly aligns the reconstructed total billed amount with the observed total billed amount for each individual household-month. (We cannot do the same for TOU household-months because we do not observe the on-peak/off-peak breakdown of total usage. We can also not perform the calculation for months in which there was no rate change from the previous month.) A few households chronically had weights outside the sensible 0-1 range in the months for which weights could be calculated, and have been dropped completely from all analysis; a few remaining households occasionally had a month with a nonsensical weight,

in which case it was just the single household-month observation that was dropped.

Finally, we calculate average billing cycle weights by billing cycle-month-year group over all household-months we could calculate the initial weights for; fill in the missing month-years (i.e. months across which there were no rate adjustments) with annual averages; then apply the appropriate billing cycle-month-year average to every corresponding non-TOU and TOU household-month. (We observe which billing cycle each household was on in September 2010, and know that households are supposed to always stay on the same billing cycle.)

We need to account for billing cycles in the imputation of on-peak and off-peak usage for the TOU household at the threshold. We align billing-month estimates with calendar-month rates by taking a weighted average of the latter across the relevant months. The weight we use in the calculation must be the billing cycle weight for a TOU household *at the threshold*. This is furnished by once more applying 2SLS estimation to equations (11)-(12), this time with average billing cycle weights as the outcome variable of interest.

We estimate total expenditure based on bundled generation-inclusive rates in a similar fashion. We first impute on-peak and off-peak usage levels *by individual TOU household-month* based on the method described in the previous section and unbundled rates aligned to billing months using the average billing cycle weights. We then align calendar-month bundled rates to billing months for all household-months, once again using the average billing cycle weights. Finally, we use the weighted bundled rates and observed total usage (for non-TOU household months) or imputed peak and off-peak usage (for TOU household months) to estimate what the total generation-inclusive billed amount would have been had each household had the utility as supplier in addition to distributor. Expenditure levels *at the threshold* based on bundled rates are then estimated via the usual application of 2SLS to equations (11)-(12), with these constructed billed amounts as the dependent variable.