

(Mis)understanding prices: How consumers respond to nonlinear electricity tariffs

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Nonlinear pricing, whereby the price is higher once usage passes a specific threshold, is a common tariff used in residential electricity contracts. The premise is that large users facing a higher marginal cost will conserve. But if consumers are inattentive to both the rate and their usage, the efficacy of such a tariff is questionable. This paper takes seriously another possibility: that consumers misunderstand the tariff. Using a rich dataset exploiting a natural experiment in British Columbia, Canada, this paper combines reduced form and structural methods to uncover heterogeneous consumer behavior. The result suggests that while a majority of households respond to average prices, and change very little, a small share of misperceiving households drives the aggregate conservation result. This finding highlights the important role misperception can play in consumer responsiveness to nonlinear pricing.

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