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IN THIS ISSUE

Cost Recovery for Low-Income Rate Affordability: Many Options Exist

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NOTE TO READERS

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Utility Companies Adopting Low-Income Rate Affordability Programs have Many Options through which to Seek Cost Recovery.

In recent comments provided to the Maryland Office of Peoples Counsel regarding the design of an appropriate statewide response to ongoing low-income affordability problems, Fisher, Sheehan & Colton (FSC) presented an overview of the mechanisms used by utilities in various states to recover the cost of providing rate affordability assistance.

In no order of significance, the options include but are not limited to the following:

California

California utilities "receive reimbursement on a dollar-for-dollar basis of all bill subsidies" provided to low-income customers.[1] California utilities use what are called "two-way balancing accounts" through which to recover their CARE expenditures.

> Two-way balancing accounts allow the utility to recover actual program costs that may be higher than the amount of funding authorized, subject to audit or reasonableness review. One-way balancing accounts limit total recovery to the authorized funding

[1] Interim Opinion on Approving 2005 Low Income Energy Efficiency (LIEE) and California Alternative Rates for Energy (CARE) Programs for Pacific Gas and Electric Company, Southern California Edison Company, Southern California Gas Company, and San Diego Gas and Electric Company, Docket R-04-01-006 et al., at 38, Decision 05.04.052, issued April 21, 2005; see also, Opinion Approving 2006-2007 Low Income Programs and Funding for the Larger Energy Utilities and Approving New Low Income Energy Efficiency Program Measuers for 2006, Docket R-04-01-006, Decision 05.12.026, at 35, issued December 15, 2005.

level. The large investor-owned utilities (PG&E, SCE, San Diego Gas & Electric Company and Southern California Gas Company) have two-way balancing accounts for CARE administrative and subsidy costs. These costs are particularly difficult to forecast accurately in advance, due to the open-ended nature of program eligibility (i.e., anyone who qualifies for the programs is entitled to participate).[2]

One advantage of the two-way balancing accounts, the commission said, is that the state's utilities can "increase their efforts, as needed, to meet (and exceed) their minimum CARE penetration targets."[3]

The costs of the California rate affordability program are passed through to nearly all customer classes.[4] The forecast program cost is divided by the forecast value of non-exempt electricity sales and volume of transported gas. To assure that program participants are not charged with the cost of the program, the discount rate is set before the surcharge is determined through which program costs are recovered. Costs are recovered on a volumetric basis.[5]

Maine

Perhaps one of the most significant developments in the Maine Public Service Company (MPS) PowerPACT program was its system of cost-recovery. The Commission approved the creation of a PowerPACT reserve.

> By establishing this reserve, both MPS and its ratepayers will be protected against significant departures between the PowerPACT allowances included in rates and actual cost expenditures. MPS shall design this PowerPACT reserve account to automatically account for differences between the cash flows received from ratepayers to fund the reserve (e.g., 0.54% of Maine-jurisdictional electric revenues) relative to the amount expended for the PowerPACT program costs. Any reserve surplus will be treated as a deduction from rate base on future rate cases. Net reserve deficiencies, if this situation were to occur, would be treated as a rate base addition in future years.[6]

In its inaugural year, the deferred account would equal 0.54% of Maine jurisdictional revenues from the last calendar year prior to the PowerPACT program year. The deferred account would be collected in rates "subject to the standard prudence review" and as an addition to rate base. "Thereafter, expenditures that exceed or fall short of the deferred account will be added to or deleted from rate base in a subsequent rate case."[7] The Commission made clear, however, that only benefits given, not administrative costs, were to be included in the deferred account.

Ohio

The issue of PIPP cost recovery is resolved by statute for Ohio electric utilities. In 1999, the Ohio legislature created a "universal service fund" that was for "the exclusive purposes of providing funding for the low-income customer assistance programs and for the consumer educa-

[2] In the Matter of the Application of Southwest Gas Corporation for Authority to Adjust Public Purpose Program Surcharges, et al., D.03-03-007, at 39, California PUC (March 13, 2003), *citing* D.02-09-021, at 7 – 9 (establishing the rationale for CARE balancing accounts).
[3] D.03-03-007, supra, at 48.
[4] Exempted from paying CARE costs are CARE customers, customers with special contracts negotiated before September 1989, utility electric generation customers, and miscellaneous small customer classes (such as street lighting).
[5] D.89-09-004, at 19 – 20, California PUC (1989). Investigation on the Commission's Own Motion to Comply with Senate 987 and Realign Residential Rates, Including Baseline Rates, of California Energy Utilities. The Interim Option, Decision 89-07-062 was issued July 19, 1989. The Final Opinion, D.89-09-844, was issued September 7, 1989. An Order on Petition for Modification, D.89-11-018, was issued September 29, 1989.
[6] Re. Investigation of Modifications to Maine Public Service Company's PowerPACT Program for the 1993-1994 Program Year, Order, at 6, Docket No. 93-158 (Maine PUC 1993).
[7] Id., at 6 – 7.

tion program" in Ohio, including administrative costs.[8] Under the statute, the universal service fund was to include revenues from a variety of sources dedicated exclusively to a statutory universal service fund. Natural gas utilities remain responsible for the management of natural gas PIPP under rules promulgated by the Public Utilities Commission of Ohio (PUCO). Cost recovery for the delta revenue is through a PIPP Rider which is embedded in distribution rates. Utilities file to increase or decrease the rider based on their judgment regarding the need to adjust revenues to cover the shortfall in customer payments.

Oregon

As part of the legislative approval of a move to electric restructuring in Oregon, the state legislature enacted statutory language explicitly creating a universal service fund.[9] The legislature declared that the program was created:

> . . .for the purpose of providing low-income bill payment and crisis assistance, including programs that effectively reduce service disconnections and related costs to retail electricity customers and electric utilities. Priority assistance shall be directed to low-income electricity consumers who are in danger of having their electricity service disconnected.[10]

The Oregon fund applies only to the state's two investor-owned electric utilities: Portland General Electric and PacifiCorp. Funding is collected from all retail customers of these investor-owned electric companies.[11] Residential customers pay a monthly meters charge, while non-residential customers pay a per kWh charge.[12] The contribution of any individual non-residential customer, however, is capped at $500 per year per "site" for each customer.[13] The Oregon Public Utilities Commission (OPUC) is charged with the responsibility of setting both the meters charge and kWh charge to generate the annual funding of $10 million.[14] The OPUC determines the distribution of the $10 million between the residential and non-residential customer classes, as well as the individual charges. In reaching this decision each year, the OPUC considers periodic filings by the two utilities based on the utilities' most recent load forecasts.[15]

Pennsylvania

Pennsylvania is unique in its recovery of program costs for its "universal service" programs (e.g., rate assistance, usage reduction, assistance referrals, LIHEAP outreach) in that it limits cost recovery exclusively to the residential class.[16] The PUC relied on two lines of reasoning to support its decision:

> The Commission believes that we should not initiate a policy change that could have a detrimental impact on economic development and the climate for business and jobs within the Commonwealth.[17]

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[8] O.R.C., §4928.51 (2007).

[9] Popularly known as Senate Bill 1149, the Oregon low-income program was codified at ORS, § 757.612 et seq. (2007).

[10] ORS, §757.612(7)(d) (2007).

[11] See generally, Oregon *Energy Assistance Program, Report to the 74th legislative Assembly*, Oregon Housing and Community Services, December 31, 2006. The statute provides that "the Oregon Housing and Community Services Department shall prepare a biennial report to the Legislative Assembly describing program spending and needs for low-income bill assistance." ORS, § 757.612(2) (2007).

[12] Under the statute, "The commission shall determine each electric company's proportionate share of the total amount. The commission shall determine the amount to be collected from a retail electricity consumer. .." ORS, §757.612(7)(b) (2007).

[13] ORS, §757(7)(b) (2007).

[14] ORS, §757.612(7)(b) (2007).

[15] See generally, ORS, §757.205 (2007; see e.g., Portland General Electric's Advice No. 02-25 and PacifiCorp's Advice No. 02-028 (December 2, 2002) (to go into effect January 1, 2003) (setting meters charge at $0.38 per month and kWh charge at $0.038/kWh); Portland General Electric's Advice 05-002 and PacifiCorp Advice 05-003(to go into effect April 1, 2005) (setting meters charge at $0.33 and kWh charge at $0.033/kWh).

[16] Pennsylvania PUC, Docket No. M-00051923, Customer Assistance Programs: Funding Levels and Cost Recovery, Final Investigatory Order, adopted October 19, 2006.

[17] Final Investigatory Order, at 31.

* * *

> [L]ess than two years ago, the Commission held that "[u]niversal service programs, by their nature, are narrowly tailored to the residential customers and therefore, should be funded only by the residential class."[18]

In adopting this approach to impose costs on the residential class only, the Pennsylvania PUC noted, but did not explain, its divergence from the mainstream. The PUC noted, however:

> The [state Office of Consumer Advocate] OCA undertook an extensive review of how costs for low-income rate assistance programs were recovered in other states. The OCA found that 26 states had CAP programs where the cost of such programs is recovered, in whole or in part, directly from increased utility charges to other ratepayers. The five largest (excluding the Commonwealth that ranks number 2) programs are California at $453 million; Ohio at $200 million; New Jersey at $160 million; Illinois at $65 million; and Massachusetts at $48 million. Of these five programs, the recovery of program costs is assessed to all customer classes. Costs are recovered through a variety of mechanisms: a public purpose charge, a rider, a volumetric charge, and a flat fee per month. Fourteen other states spread the cost of CAP programs across all customer classes, including Arizona, Connecticut, Indiana, Maryland, Michigan, Minnesota, Nevada, New Hampshire, New York, Oregon, Rhode Island, Utah, Washington and Wisconsin. Three states, Georgia, Maine and Montana, fund programs by utility profits. The remaining three states fund programs by assessments on residential ratepayers only. These three programs are funded at less that $2 million each.[19]

The PUC finally did not accept the OCA's observation that the benefits of a universal service program did not reside exclusively in the residential class. According to the OCA, "The small businesses that pay low wages indirectly rely on the utility's willingness to make up the difference between those wages and what it costs employees to live. Requiring all customer classes to help pay for universal service programs that respond to inability-to-pay resulting from the payment of low wages is simply one mechanism to have the customer classes which benefit from the universal service program pay some part of the cost of that program."[20]

The Pennsylvania PUC adopted a cost recovery mechanism that allows utilities to recoup the costs of their universal service programs through a reconcilable surcharge. The PUC noted that this policy was a change from its historical approach. According to the PUC, the use of a reconcilable surcharge was attributable to the unique statutory framework for universal service programs in Pennsylvania:

> In [previous] cases, the Commission rejected the argument of the utilities for full cost recovery via a reconcilable surcharge. Instead, the Commission agreed with the argument of [PUC Staff] and OCA to recover CAP expenses through base rates, an approach that. . .does not assure full cost recovery.
>
> Against this historical backdrop, the General Assembly approved the Competition Acts that made universal service programs mandatory, and that expressly mandated "full recovery" of the related costs. It is reasonable to conclude that the General Assembly did not intend "full recovery" of universal service costs to mean that the

[18] Id., at 31, quoting *Pa. PUC, et al v. PPL Electric Utilities Corp.*, R-00049255, 2004 Pa. PUC Lexis 40 (December 22, 2004).

[19] Final Investigatory Order, at 28, citing OCA Comments at 24 – 46.

[20] Final Investigatory Order, at 27 – 28.

> Commission could continue its previous practice and only allow recovery of such costs through base rates. The reasoning that CAP costs "are no different from any other cost" echoes the arguments of [PUC Staff] and OCA in cases that predate the statutory requirement for "full recovery" of universal service costs. In short, CAP costs are different from other expenses in that the General Assembly has mandated "full recovery" of these costs.[21]

The PUC noted that "requiring utilities to recover CAP costs through base rates would be returning to the cost recovery policy followed by the Commission prior to the General Assembly's requirement of full cost recovery."[22]

Wisconsin

The Wisconsin state utility commission developed an inventory and valuation of the dollars expended by Wisconsin utilities for low-income energy assistance in a 2000 proceeding.[23] According to the commission, Wisconsin utilities provided $21.3 million in low-income assistance, including "low-income weatherization, low-income uncollectibles and arrearages, and low-income Early Identification Programs (EIP)."[24] In making this determination, the commission found that "the historical assumption that 50 percent of total uncollectibles is attributable to low income households is not determinative." In addition, the commission found, "it is not reasonable to base an estimate of low-income uncollectibles solely on participation in the federal Low-Income Home Energy Assistance Program."[25]

In its 2000 Act 9 proceeding, the commission decided that some programs operated by Wisconsin's utilities in 1998 would continue to be operated by the utilities even after the advent of the public benefits funds. Rather than transferring the dollars used on those programs to the fund, the commission said, those dollars would be left with the utilities to continue the program.

The Early Identification Program (EIP) was one such program. "Utilities will continue to be the first point of contact for their customers and the utilities will have to continue to assist these customers through EIP services."[26] Until ordered by the commission to do otherwise, "each utility shall continue to spend annually, at a minimum, a level of funding equivalent to the retained portion of its 1998 EIP expenditures."[27] If funds were not spent on "appropriate EIP-related activities," the commission said, those dollars should be transferred to the commission for deposit in the utility public benefits fund.[28]

In addition, the Commission found that "voluntary customer and corporate contributions to utility-sponsored customer assistance programs are not considered utility public benefits expenditures for purposes of establishing 1998 utility expenditures levels."[29] Finally, the commission determined that "customer service activities are distinct from utility public benefits programs."[30]

Cost recovery for the dollars each utility transfers to the public benefits fund is accomplished in Wisconsin through base rate case proceedings.[31] According to the commission "if a utility requests rate recovery for public benefits-related costs that they are required to transfer to DOA, the utility will need to justify the need for rate recovery in its rate case proceeding."[32]

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[21] Final Investigatory Order, at 16-17.
[22] Final Investigatory Order, at 16-17.
[23] Investigation on the Commission's Own Motion of Appropriate Measures to Maintain or Enhance the Existing Levels of Energy Efficiency, Services to Low-Income Customers, Renewable Resources and Research and Development ("Public Benefits") in Restructured Electric and Natural Gas Industries, Docket No. 05-BU-100, Decision (August 17, 2000). (hereafter, Act 109 Order).
[24] Act 9 Order, at 3.
[25] Act 9 Order, at 4.
[26] Act 9 Order, at 11.
[27] Id.
[28] Act 9 Order, at 15.
[29] Act 9 Order, at 8.
[30] Act 9 Order, at 5.
[31] January 2001 Act 9 Order, at 12.
[32] January 2001 Act 9 Order, at 13 ("it is reasonable to address the specific rate recovery issues identified by the util-

The Wisconsin public benefits fund is also to be supported by a "low-income assistance fee" to be imposed on all customer bills.[33] While the amount of the charge is to be determined by the Department of Administration each year, the statute provides that the charge is to be a fixed charge,[34] and that customers shall be given an annual summary of the money they have paid through the charge and the programs supported by the charge.[35] The statute provides that all customer classes must pay the fee, with 70% of the total revenue being collected from the residential customer class and 30% being collected from non-residential customers.[36]

The amount of the low-income assistance fee is to be established such that, when combined with the other low-income resources (identified above), the sum equals the "low-income need" in the state of Wisconsin.[37] "Low-income need" is defined to mean the "amount obtained by subtracting from the total low-income energy bills in a fiscal year the product of 2.2% of the estimated average annual income of low-income households in this state in that fiscal year multiplied by the estimated number of low-income households in this state in that fiscal year."[38] Estimates of low-income home energy bills are based on data obtained from the state energy agency.[39]

ities and any others yet to be identified in future rate case proceedings"). Id.

[33] Wisc. Stat. §16.95(4)(a) (2007).

[34] Wisc. Stat., §16.957(4)(b) (2007). The fees shall be established by DOA regulation and shall not be imposed on a per kilowatthour basis. Wisc. Stat. §16.958(4)(b) (2007).

[35] Wisc. Stat. §16.957(4)(am) (2007).

[36] Wisc. Stat. §16.957(4)(b)(2) (2007).

[37] Wisc. Stat. §16.957(4)(c) (2007).

[38] Wisc. Stat. §16.957(1)(n) (2007). In turn, "low-income energy bills" "Total low-income energy bills" means the total estimated amount that all low-income households are billed for residential electricity, natural gas and heating fuel in a fiscal year. Wisc. Stat. §16.957(1)(u) (2007).

[39] Wisc. Admin. Code, Admin. §43.04(1) (2007).

New Jersey

The New Jersey commission approved the collection of universal service costs through a system benefits charge. Under this SBC, the difference between actual SBC costs and SBC recoveries will be subject to deferral. The SBC will be reset annually to amortize the over- or under-recovered balances and to provide for current program cost recovery over the ensuing year.[40]

The New Jersey's utilities have repeatedly requested the authority to implement "self-implementing" intra-year changes in the SBC, under which the SBC could be changed on 30-days notice. The utilities have argued that "it has been difficult to arrive at the proper level for USF rates because a number of variables that impact the calculations have a high degree of uncertainty. These uncertain variables include the rate at which customers will be successful in earning forgiveness under the arrearage payment program, known as the Fresh Start program; the number of customers who will be enrolled during the final automatic enrollment sweep; and the rate at which customers will apply for the program once the direct application system, formerly called the manual enrollment system, is complete."[41] The New Jersey commission has yet to approve that self-implementing cost recovery mechanism.[42]

[40] See, e.g., In the Matter of Rockland Electric Company's Rate Unbundling, Stranded Cost and Restructuring Filings, BPU Docket No. EO97070464, EO97070465 and EO97070466 (consolidated), Final Decision and Order, at 34, 63 (July 22, 2002); In the Matter of Public Service Electric and Gas Company's Rate Unbundling, Stranded Costs and Restructuring Filings, BPU Docket Nos. E097070461, E097070462 and E097070463 (consolidated), Final Decision and Order, at 111 (August 24, 1999).

[41] In the Matter of the Establishment of a Universal Service Fund Pursuant to Section 12 of the Electric Discount and Energy Competition Act of 1999, Docket No. EX00020091, Universal Service Fund Order Approving New USF Program Year Rates and New Lifeline Rates, at 2 (June 23, 2004).

[42] See e.g., In the Matter of the 2006/2007 Annual Compliance Filings for the Universal Service Fund Program Factor within the Societal Benefits Charge Rate Pursuant to Section 12 of the 1999 Electric Discount and Energy Competi-

Finally, the commission decided that it would "segregate the USF revenues and benefits for gas and electric customers such that the total USF recoveries from gas customers will be used to provide payment assistance to gas customers and the total revenue recoveries from electric customers will be used to provide payment assistance to electric customers."[43]

Nevada

Though similar in structure, the bill payment assistance in Nevada differs somewhat in purpose from that distributed in related programs in other states. Like many states, Nevada pays percentage-of-income based benefits to its program participants. The Nevada program is, however, not aimed at making bills affordable. Instead, it has more of an equity emphasis to it. Rather than tying bill payment assistance to an affordable percentage of income, the Nevada statute provides that the amount of assistance provided to each household shall, to the extent practicable, be "sufficient to reduce the percentage of the household's income that is spent on natural gas and electricity to the median percentage of household income spent on natural gas and electricity statewide."[44] The percentage of income home energy burden for the median-income household, in other words, was, by law, deemed to be the objective of the program irrespective of whether that median income burden is above, below or precisely equal to that which is affordable.

The Nevada low-income energy assistance programs are funded through a legislatively-imposed "universal energy charge."[45] The universal energy charge is imposed on "each retail customer,"[46] which is explicitly defined to include "without limitation, a residential, commercial or industrial end-use customer that purchases natural gas or electricity for consumption" in the state.[47] While customers of certain types of utilities are exempt from paying the universal energy charge,[48] those customers are also prohibited from receiving any "money or other assistance" from the universal energy fund.[49]

The Nevada statute is specifically designed to impose the universal energy charge on customers that have bypassed the distribution systems of the state's electric and/or natural gas utilities. In the event that a customer uses the distribution system of the local public utility, the utility is directed to collect the universal service charge as a separately stated line-item on each customer's distribution bill.[50] If a retail customer does ***not*** use the local distribution utility, however, the statute imposes the responsibility on each such customer to remit the appropriate funds to the state.

The Nevada program is designed so that the program funding is set by statute, rather than fluctuating to meet the required needs of program participants. A uniform charge of 3.30 mils per therm of natural gas, and 0.39 mils per kWh of electricity, is imposed on each retail cus-

tion Act of 1999, Docket No. ER06070525, Order Approving Interim USF Rates and Lifeline Rates, at 9 (October 23, 2006). ("The Board is not convinced that there is any reason why an adjustment would need to be self-implementing. If the [electric distribution companies] or [gas distribution companies] believe it is necessary to adjust USF rates prior to the annual July 1st filing period, they may make appropriate filings with the Board, with a copy to Rate Counsel, and the Board will consider such adjustment." Id., at 9.

43 2003 USF Order, at 7. "Any excess or deficient revenues for either sector based on the benefits paid out would be carried forward to the subsequent year's budget for the corresponding group of customers, which would more directly match payments made to gas customers with the associated recoveries from gas customers." Id.

44 N.R.S., §702.260(6)(a) (2007).

45 N.R.S., §§ 702.100 (2007) and 702.160 (2007).

46 N.R.S. §702.160(1) (2007).

47 N.R.S., §702.090(2) (2007).

48 For example, customers of Rural Electric Cooperatives (RECs) do not pay the universal service charge. This statutory mandate, however, was largely rendered irrelevant by program provisions that allowed customers of such utilities to receive greater LIHEAP benefits, with the reduction in LIHEAP benefits in the rest of the state being made up out of universal service funds.

49 N.R.S., §702.150 (2007).

50 N.R.S., §702.160(3) (2007).

tomer.[51] Statutory caps were created, however, on the quarterly payment that any single customer or "multiple retail customers under common ownership and control" are required to pay.[52] The only role played by the Nevada utility commission in the administration of the state's universal service program is the administration of the imposition and collection of the funding.

Given the limited funding provided under the Nevada statute, the program administrators are given flexibility in defining both what population they are to serve and precisely what amount of assistance –as opposed to what *type* of assistance—they are to provide. The Welfare Division may provide assistance to households with annual income of "not more than 150% of the federally designated level signifying poverty. . ."[53] In times of constrained funding, therefore, it would appear that the Welfare Division could limit eligibility below this level if needed to stay within budget. Moreover, the Welfare Division's obligation to distribute bill payment assistance to reduce home energy burdens to that of the statewide median is only "to the extent practicable."[54] In times of constrained funding, it may not be "practicable" to achieve that statutory objective.[55]

Finally, while the Welfare Division is "*authorized* to render emergency assistance to a household if an emergency related to the cost or availability of natural gas or electricity threatens the health or safety of one or more of the members of the household,"[56] it is not *required* to render such emergency assistance. In times of constrained funding, it may choose not to exercise those actions which the program's statutory charter authorizes but does not mandate.

SUMMARY AND RECOMMENDATIONS

For more information on the costs and benefits of low-income rate affordability programs, including program cost recovery, readers may send requests to:

roger[at]fsconline.com

Fisher, Sheehan and Colton, Public Finance and General Economics (FSC) provides economic, financial and regulatory consulting. The areas in which *FSC* has worked include energy law and economics, fair housing, affordable housing development, local planning and zoning, energy efficiency planning, community economic development, poverty and telecommunications policy, regulatory economics, and public welfare policy.

[51] N.R.S., §702.160(1) (2007).
[52] Quarterly payments exceeding $25,000 are subject to refund under the statute. N.R.S., §702.160(5) (2007).
[53] N.R.S., §702.260(3) (2007).
[54] N.R.S., §702.260(6)(a) (2007).
[55] How the Welfare Division would *actually* respond to funding constraints is, of course, speculative. Whether the Division would reduce benefit levels (by increasing the percentage of income burden) or reduce eligibility, or engage in some other action, cannot be determined in the abstract. This discussion only identifies what the Division is *authorized* to determine.
[56] N.R.S., §702.260(4) (2007).