Universal System Benefits Charges:  
The New Regulatory Imperative for Avoiding Stranded Benefits  

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The nation's utilities generally are concerned that they could soon be plunged into a competitive arena dominated by short-term electric commodity prices. As a result, some utility managers have concluded that any investments that raise those prices -- however slightly -- could result instantly in the loss of customers and revenues. This helps account for utilities' nervousness about long-term investments of all kinds, and their particular concerns about electricity-saving and renewable energy initiatives. The result, in NARUC's phrase, is large and growing "stranded benefits" from what would have been highly cost-effective investments.¹

The issue today is not whether utilities are right in their concerns about the future; many join NRDC in working for a very different and more environmentally responsible outcome. But no one can eliminate the threat overnight; it is now clear that the restructuring debate will extend over a period of years. State regulators and publicly-owned utilities need a near-term strategy that can sustain progress on crucial long-term investments while that debate proceeds.

The solution lies in converting cost recovery for energy efficiency, low-income services and R&D to a non-bypassable, usage-based "system benefits charge" on electric distribution services. Cost-effective renewable energy acquisitions should also qualify to the extent that their initial cost streams exceed short-term commodity costs. This would create a cost-recovery structure that can accommodate strong performance-based incentives and retain consistency with all plausible restructuring outcomes. Washington's Utilities and Transportation Commission recognized as much in December of 1994 when it approved

¹The National Association of Regulatory Utility Commissioners (NARUC) passed a resolution on "stranded benefits" at its November 1994 annual meeting in Reno, NV. Included among the utility system's "potentially stranded benefits" were "systematic investments in energy efficiency", "meeting the specific needs of low-income customers", "system reliability and fuel diversity", and "research and development for the electric industry." NARUC concluded that "it is the responsibility of state and federal electric utility regulators to assure that these vital public benefits are not 'stranded', but are well-served in new electric industry structures and in the transition to them." Resolution on Competition, the Public Interest, and Potentially Stranded Benefits (November 14, 1994).
Washington Water Power's proposal for a usage-based distribution charge to recover energy-efficiency investments. Idaho followed in March of 1995. A broad coalition of California-based groups has also endorsed this approach in a statement filed with the California Public Utilities Commission, and many other states, utilities and organizations are exploring the concept.

The recommended cost-recovery system requires no change in current rates or rate structures. Utilities today typically recover "stranded benefits" charges from all distribution system users based on volume of consumption; they would continue to do so under the new system. The only difference is that state commissions and publicly-owned utilities would make explicit (as Idaho and Washington now have) that distribution system users cannot bypass their share of contributions to stranded benefits by designating a new supplier of kilowatt-hours over the integrated grid (assuming that states ever decided to permit this). Questions and answers follow regarding implementation issues.

1. **Is it clear that states and publicly-owned utilities have authority to adopt universal system benefits charges for users of electrical distribution systems?**

Yes. The Federal Energy Regulatory Commission (FERC) acknowledges state ratemaking authority over distribution services (the boundary between state-regulated distribution and FERC-regulated transmission is blurred, but no one disputes its existence). The "stranded benefits" initiatives themselves, and cost recovery for them, have been mainstays of state and local utility regulation for the past two decades.

In a March 29, 1995 Notice of Proposed Rulemaking, FERC explicitly endorsed state and local regulators' right to use distribution charges to avoid "stranded benefits" from utility investments in energy efficiency. The agency confirmed that nonfederal regulators "may also use their jurisdiction over local distribution facilities to address potential 'stranded benefits', e.g., environmental benefits associated with conservation, load management, and

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^Washington Water Power (WWP) filed its distribution charge proposal with the Washington Utilities and Transportation Commission on October 25, 1994; Commission approval came in December (DSM Tariffs UE-941375 & UE-941377). The Idaho Commission endorsed a virtually identical WWP proposal in Order No. 25917, Case No. WWP-E-94-10 (March 6, 1995).

^The "Joint Statement on Electricity Usage Charges" (March 10, 1995) recommends "a non-bypassable electricity usage charge which would be applied to each utility's customers" and "would be used to sustain cost-effective investments by utilities and third parties that provide demand-side management services (DSM), renewable technologies, research and development (R&D), and low-income services." Signers included low-income service providers, environmental groups, the Greenlining Institute, the National Association of Energy Services Companies, the Pacific Gas & Electric Company, and the Sacramento Municipal Utility District.
other demand side management (DSM) programs. FERC implies a broader reach for the concept by citing NARUC’s resolution on "stranded benefits", which covers R&D, renewable energy and low-income services (see note 1 above).

2. **Is this cost recovery approach consistent with the concept of energy conservation as a least-cost resource for utilities?**

   Certainly. Indeed, it is precisely the system-wide resource benefits delivered by cost-effective conservation that help justify its inclusion in a system benefits charge. The proposal is to change the characterization of cost recovery for conservation and other system-benefits investments, not to reconsider the rationales underlying those investments.

3. **Wouldn’t these charges encourage bypass?**

   Complete physical bypass of an integrated grid is both rare and costly; shifting the basis of cost recovery for "stranded benefits" certainly won’t make it any more attractive than it is now. Most talk of "bypass" today involves the retail wheeling variety, which does not involve physical disconnection from the grid and would not affect customers’ obligation to pay distribution charges. Also, as a recent report to the California Public Utilities Commission indicates, distribution charges need not be limited to customers at or below a specified voltage level.5

4. **How big would the charge have to be?**

   That is a decision that should be made on the basis of each system’s resource and other needs, but on average charges would not exceed five percent of current bills. Utilities should invest no more — and no less — than is needed to minimize system-wide life-cycle costs of reliable energy services, while ensuring equitable treatment of low-income customers.

5. **Isn’t this just a new tax for social programs?**

   No -- state commissions are dealing here with cost recovery for investments that are crucial to sustaining high quality electric service. States can and should continue to build in strong performance-based incentives to deliver system value at least cost. In general, non-bypassable charges should be reserved for investments that can be shown to represent

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4 See 60 Federal Register 17662, 17691 n. 230 & 17711 n. 304 (April 7, 1995).

5 Working Group Report: Options for Commission Consideration, pp. iii & 66 (Feb. 22, 1995) (more than 100 highly diverse parties to California’s utility restructuring proceeding assisted with this report, which the Commission had formally requested).
potential "stranded benefits" for electrical systems. General purpose social programs don’t belong here any more than they belong in electricity bills generally.

6. **Does a universal system benefits charge require a change in current practice for amortizing conservation costs or assigning them to customer classes?**

   No; such an approach can be adapted to either multi-year amortization of costs or year-by-year expensing, and it need not affect current cost allocations.

7. **Does adopting a universal system benefits charge signal a preference for or against retail wheeling?**

   No. It signals only a strong preference for avoiding stranded benefits in an era of widespread uncertainty about the electric industry’s ultimate structure.