

## Minimizing Rate Impacts of Efficiency Programs

### ISSUE SUMMARY:

Imagine if you had to pay for the poles and wires that carry electricity to your home in the first year that they were built.

If we had to pay for things like that, then we wouldn't be able to afford many of them.

Unfortunately this is the way we pay for our energy efficiency programs in Texas—upfront.

Even though energy efficiency is the cheapest and cleanest source of energy available, the way we pay for energy efficiency programs makes their short-term rate impacts artificially high. We need to find ways to encourage more energy efficiency while minimizing rate impacts.

One solution is a financing mechanism that would spread a program's costs over the time that it provides benefits, which is typically 10-20 years or more for efficiency measures (e.g., insulation, efficient air conditioners).

### EXAMPLE:

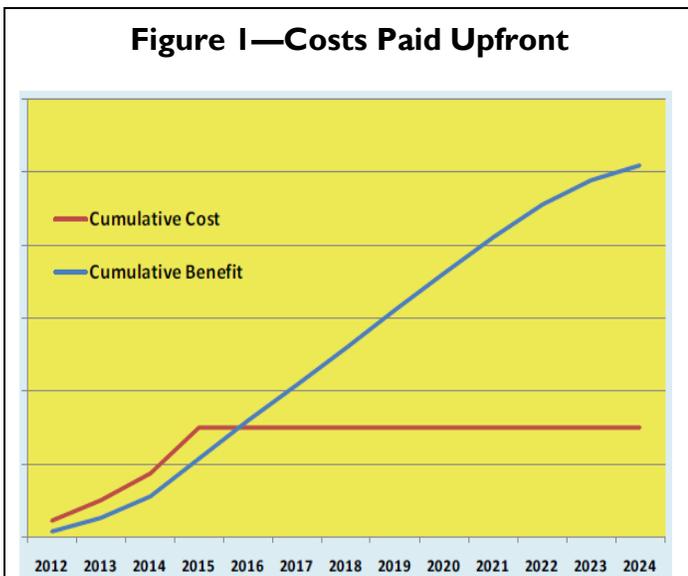
The example in Figure 1 below shows the current way of paying for programs. Program costs are paid by utilities upfront and ratepayer benefits accrue over time. In this example, new programs are launched in 2012-2015 (accruing costs) while benefits last through 2025; the programs do not break-even until four years after inception.

Figure 2 shows the same level of spending, but the costs have been spread over the useful lives of the improvements along with a conservative estimate of finance charges (9%). With the costs spread over time, the programs immediately break-even, and there is no “rate-shock” for consumers.

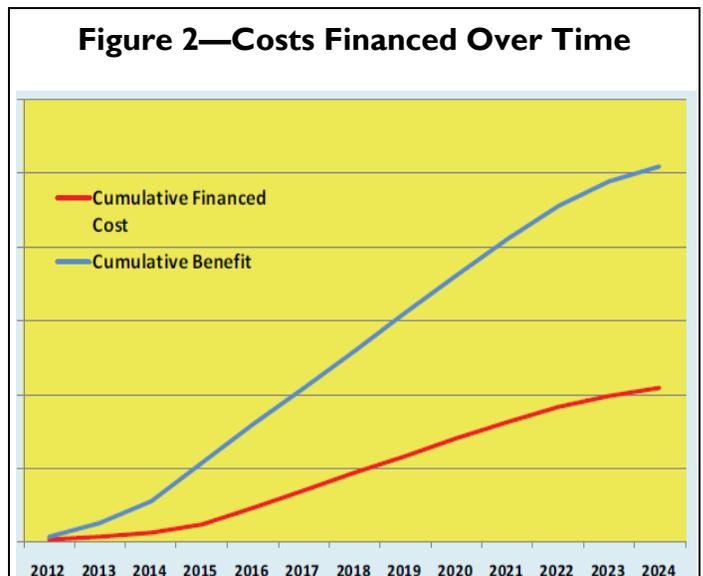
### KEY POLICY CONSIDERATION:

- A financing mechanism should be made available to minimize the rate impact of energy efficiency programs to consumers by spreading the program costs over time, like the way transmission infrastructure is financed.

**Figure 1—Costs Paid Upfront**



**Figure 2—Costs Financed Over Time**



## TALKING POINTS:

- If ratepayers had to pay for transmission infrastructure upfront, we couldn't afford many new poles or wires. The same is true with homes, cars, cellular networks, and other large investments. Efficiency programs are no different.
- If you had to pay for 10 years of iPhone service upfront, an iPhone would cost over \$9,000 (\$75/month \* 120 months).
- Financing spreads out the costs, making efficiency a net positive to consumers from day one.
- With a 10-year financing mechanism, \$1.30 in efficiency program costs could become closer to \$0.13.
- Financing energy efficiency programs would allow them to be expanded greatly while lessening the rate impact for consumers.
- Expanding the programs would create jobs that cannot be outsourced and lower electricity bills for all Texans.

## OPPONENTS SAY:

- *"Efficiency program costs are incurred in the first year, so they should be recovered in the first year."*

RESPONSE: Because the costs of generating energy are financed over time while efficiency programs are not, this inadvertently provides an unfair advantage for traditional utility services, which makes the best, most cost-effective choice—energy efficiency—less attractive. A financing mechanism will allow utilities to recover their costs upfront, but will spread the expenses over time, putting efficiency on a level playing field with generation.

- *"Financing efficiency programs will add to the overall costs."*

RESPONSE: Just as the total cost of buying a home is higher with financing, the overall cost of the programs would be too. However, the overall costs are still much lower than the overall benefits. The example on the front of this page includes a conservative estimate of 9% in financing costs.

## BACKGROUND AND HISTORY:

Utilities originally rolled energy efficiency program costs into their rate bases. The option to continue this practice was maintained when the Texas electricity market was restructured in 1999 (SB 7 in the 76th Regular Session).

However, more recently adopted rules, including updates to the efficiency programs made by HB 3693 in 2007, allow the utilities to recover all their efficiency program and incentive costs in the same year that the program expenditures take place, and they have chosen to do so. The effect of these changes is to drive the annual efficiency program expenses directly into consumer rates each year.

There is nothing in statute that explicitly prevents utilities from financing efficiency programs, but with the establishment of the cost recovery factor that allows utilities to recover all costs immediately, the utilities will likely not do it without legislative action.

Effectively financing efficiency could allow the State to raise its efficiency goals significantly and achieve great savings for ratepayers. While small incremental increases to efficiency programs can be made absent financing, increases large enough to significantly lower electricity costs will require a financing mechanism to lower the short-term rate impacts.

## RESOURCES AND CITATIONS:

National Action Plan for Energy Efficiency (2009). *Discussion of Consumer Perspectives on Regulation of Energy Efficiency Investments.*

[www.epa.gov/eeactionplan](http://www.epa.gov/eeactionplan)

See pages 5.1-5.2 for discussion of financing.

State Energy Conservation Office (October 2008). *The Home Energy Efficiency Report.*

[http://www.window.state.tx.us/specialrpt/hb3070/96-1350\\_Home\\_Energy\\_Eff\\_HB3070.pdf](http://www.window.state.tx.us/specialrpt/hb3070/96-1350_Home_Energy_Eff_HB3070.pdf)