IGU Conversions Program

2017 Program Update

Prepared for:
Jomo Stewart
IGU General Manager

Prepared by:
Monique Garbowicz
Conversions Lead

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Revision	Description	Author		Quality Check		Independent Review	
Draft Rev. A	Original	M. Garbowicz		G. Turner		D. Prusak	

Sign-off Sheet

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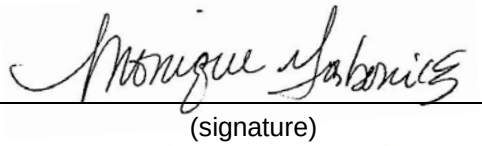
Prepared by 
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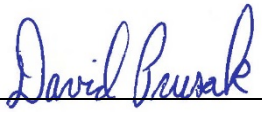
Monique Garbowicz

Reviewed/Approved by 
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David Prusak

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Abbreviations

CMU	Chambersburg, Pennsylvania Municipal Utility
EE	energy efficiency
EESI	Environmental and Energy Study Institute
FNSB	Fairbanks North Star Borough
IEP	Interior Energy Project
IGU	Interior Gas Utility
OBF	On-bill Financing
OBR	On-bill Repayment
Plan	Conversion Program Tactical Plan
Stantec	Stantec Consulting Services, Inc.

Executive Summary

This update to the Interior Gas Utility (IGU) Conversion Program Tactical Plan (Plan) progresses and refines the tactical approach and recommendations to implement the Interior Energy Project (IEP) Conversion Program. The Conversion Program will focus on residential participants, including homeowners and renters. The number and rate of residential conversions to natural gas and the on-boarding of new customers has been identified as keys to the success of the IEP.

The IGU conversion program is expected to ultimately be a function of the utility structure that results from the integration of IGU and Fairbanks Natural Gas. Other aspects of the IEP, including gas supply, utility integration plans, and due diligence activities are still in various stages of development. Also to be identified or determined are utility funding sources available for use to expand customer service offerings for conversions and on-boarding support.

With that being the case and as recommended in the previous update, the IGU Conversion Program team has focused on advancing the definition of an on-bill repayment (OBR) program and the associated legal authorizations needed to support such a program as previously recommended.

Recommendations from the previous updates presented to the IGU Board include the following:

- Continue to work to identify sources of low interest capital.
- Continue to identify attributes of successful on-bill payment programs.
- Continue legal review of financing program attributes:
    - On-bill financing (OBF)/repayment mechanism.
    - Use of rate-payer funds to support financing program:
        - Loan loss reserve.
        - Interest rate buy down.
        - Administrative costs.
    - Utility service shut-off.
    - Ability to transfer loans with property and “follow the meter” versus homeowner.
- High level OBR implementation timeline.

To support this effort, IGU is working with the Environmental and Energy Study Institute (EESI), a non-profit entity which focuses on the establishment of OBF and repayment programs to support energy efficiency initiatives. EESI provides services to municipalities and utilities free of charge, but does not provide program funding or capital.

The cost/price of gas and other consumer decision drivers, such as convenience and cleanliness of natural gas, may impact the ultimate rate of conversions but are not discussed here as program attributes. This is because they are out of the control of the IGU conversions program and corresponding OBR program.

FINDINGS

Third-party Lenders and Capital

Through additional research of other on-bill and federal funding programs, EESI confirms that there is a very low likelihood of 0% or low interest rate federal funds being available to IGU to support conversions from petroleum-based liquids to natural gas. This coupled with the State of Alaska's current fiscal challenges supports the path forward to developing an OBR program using third-party lenders and capital.

OBF Case Study - Chambersburg, PA Municipal Utility

Appendix A of this update includes a Case Study prepared with cooperation from EESI. This Case Study presents programmatic details relative to the on-bill financing program offered by the Chambersburg Municipal Utility. Similar to IGU, this program was developed to support customer conversions to natural gas. As such, attracting and bolstering conversions with the current costs differential between fuel oil and gas is also an issue for them. Also like IGU, this is in addition to any consideration of the convenience and cleanliness of natural gas.

The case study includes presentation of the general discussion and follow up questions, answers, and lessons learned. Lessons learned provide confirmation of program attributes under consideration by IGU.

Some of the program lessons learned include:

- Cost to customer of gas versus fuel oil is a primary driver.
- Positive results from strong customer service programs.
- Positive results from highly engaged contractor community.
- Utility defined creditworthiness requirements, such as utility bill payment history or credit score.

IGU On-bill Program Roles and Responsibilities

A process to identify program implementation roles and key entities was initiated to define the potential engagement of IGU on this program. Using a template typically used for this purpose by EESI, the team worked with IGU General Manager to identify the key roles and activities associated with implementing an on-bill program. Responsible parties include the utility either separately or in combination with the FNSB, and un-named third parties. Primary areas of interest include:

- Financial

- Customer Service
- On-site Activities
- Contractor Engagement
- Other Administration Activities

Legal Review

In response to a request by IGU General Manager, CSG, Inc. provided a legal review regarding potential program features, as noted above. The request was for a determination and recommendation regarding the legal authority of IGU to implement an on-bill repayment program as proposed. Generally, current Alaska statute is silent regarding on-bill financing or repayment activities. Rather than interpret or summarize the CSG, Inc. findings, the entire response is included in this document as Appendix B.

Appendix C contains examples of legislation used by other states and entities to obtain legal authority for the implementation of an on-bill program.

On-bill Program Implementation

To provide IGU and its board with an idea of the steps, and timing of those steps, associated with implementation of an on-bill program, EESI provided a high level timeline. For this timeline, which spans approximately 23 months, Year 3 is the year gas is available to IGU and the program is expected to be available to support conversions customers. Years 1 and 2, therefore present the implementation activities leading up to Year 3. It should be noted that in order for the program to be implemented, it needs to be planned and staffed accordingly. This includes legal authority and integrated operational plans, policies, and procedures necessary for implementation. Recommendations and implementation strategies for these plans, policies, and procedures will be advanced in future program development efforts.

CONCLUSION

The primary conclusions are based upon research, discussions with other utilities, and EESI on-bill program expertise. The program contemplated by IGU is similar to other customer on-boarding programs established by other utilities. As a result, other than estimating costs, no further research regarding program attributes is recommended.

Instead it is recommended that efforts be made toward the following:

- Obtaining IGU Board approval to advance detailed planning.
- Obtaining explicit legal authorization to implement an on-bill program as considered by IGU.
- Determining customer service scope of work.
- Integrating new customer on-boarding and conversions customer service program with utility operations planning.
- Determining staffing needs for –

    - New customer service program (conversions and on-boarding)
    - On-bill repayment program
- Implementing activities identified on on-bill program timeline.

1.0 INTRODUCTION

This document provides an update and overview of the ongoing effort to advance the objectives of the Interior Gas Utility (IGU) Conversion Program. Information presented and recommendations made are based upon Interior Energy Project (IEP) program data.

During this reporting period, as other elements of the IEP were defined and advanced, IGU management directed Stantec to focus effort on items that IGU could offer on its own, without additional funding resources. As a result the conversions plan was focused on attributes of an on-bill repayment program for IGU.

It is expected that this update will be included in the Conversion Program Tactical Plan (Plan), March 2016, as an appendix. The Plan is based upon several assumptions – including gas supply, the operation plan for the combined IGU and Fairbanks Natural Gas utility, and internal and external funds available to support such initiatives.

As the dates for these and other IEP related tasks change, certain conditions relative to the conversions program can also be expected to change. Financial impacts of the proposed customer on-boarding and conversions support programs, including on-bill repayment, will be estimated at a later time. First, the impacts to conversions of recently determined details relative to gas supply cost, storage and delivery, and utility integration need to be better understood and incorporated.

Thus, to advance previously reported work, the IGU Conversion Program team has focused on initiatives it can support, like OBR. This includes continuing to refine program objectives related to: (1) the potential structure and key attributes of a repayment program, (2) the necessary legal and regulatory authorizations required to execute the program as proposed, and (3) the implementation schedule for an on-bill program.

Stantec Consulting Services, Inc. (Stantec) has leveraged the energy efficiency expertise of the Environmental and Energy Study Institute (EESI) and their knowledge of developing on-bill financing and repayment systems for utilities. The team reviewed ongoing on-bill programs with respect to on-bill programs to support conversions to natural gas. In addition, the team engaged existing program administrators regarding the attributes of their respective programs, and which of those attributes contributed to program participation and success.

The overwhelming majority of utilities using on-bill programs are electric utilities and almost none support conversion to natural gas. However, the Chambersburg, Pennsylvania Municipal Utility (CMU) provides an on-bill financing program to support conversions to natural gas. Although there are differences between IGU and CMU, the CMU on-bill program supports conversions to natural gas. A case study reviewing the CMU program was developed in coordination with EESI. The case study includes a Stantec and EESI interview with CMU program administrators, and is presented in **Appendix A** of this document.

Research of successful and long term on-bill programs confirms that the intention of IGU to provide a customer-focused program to encourage and support adoption of natural gas is consistent with those programs. The proposed IGU program and the programs reviewed include the following on-bill program attributes:

- Well defined roles and responsibilities for the utility and third party participants.

- Strong Contractor engagement, which includes education regarding the on-bill program.
- High levels of customer service.
- Defined loss prevention and default protection strategies.

2.0 BACKGROUND

IGU seeks to develop a facilitated residential conversion support (new customer on-boarding) program, to be executed to coincide with when gas is available to IGU. Attributes of the "one-stop shop" program include providing:

- Customer Service
- Information
- Support

These customer-centric services would support new residential customers who sign up or on-board to the utility systems. On-boarding activities include providing service, information, and support regarding:

- Connection and conversion processes.
- Consumer lending and repayment program(s).
- Participating contractor involvement.
- Service line locations, installations, and connections.
- Installation quality assurance/acceptance.

In addition, IGU seeks to include an OBR program to bolster residential conversions by developing a program that reduces first cost impacts by extending the payback period - as this may be a significant barrier for some - and increasing the ease and convenience of adoption.

2.1 ON-BILL REPAYMENT

The option recommended for continued research and effort is a consumer loan repayment program that uses third-party capital as the source of funding for a loan program. Funds are provided to consumers by private financial institutions or public funding entities. Loans, which may be pre-qualified using utility defined metrics (utility bill payment history or credit score), are issued via payments made by the lender directly to the contractor upon completion of the work. Loan repayment is made to the lender through the utility's billing and collection processes. In this situation, the lender is the loan originator and administrator.

Typically, interest rates are passed along to the consumer and include the cost of capital, as well as any program administration costs incurred by the utility. Low interest sources of capital, such as grants or funds administered by non-profit entities, allow the loans to be issued to consumers at lower rates than traditional lending institutions.

Early program goals of obtaining low interest or zero-percent interest funds via federal sources beyond what is currently available, seem today to be highly unlikely: Current

funding programs either do not support gas utilities or fossil fuel heating unit changes from liquid to gas.

Therefore, the option recommended for development is a consumer loan repayment program that uses third-party capital. Funds are provided to consumers by private financial institutions or public funding entities. Loans, which may be pre-qualified using utility defined metrics, are issued via payments made directly to the contractor upon completion of the work. Loan repayment is made to the lender through the utility's billing and collection processes. In this situation, the lender is the loan originator and administrator, with the utility acting predominately as a pass-through mechanism for payments.

Typically, using private lender capital often results in higher interest rates to the consumer. This is true, unless:

- The utility provides a loan loss reserve or interest rate buy-down.
- A Same-as-Cash product is used and the consumer pays off the debt during the no-interest period.
- Lenders recognize the historically low default rates of EE related on-bill programs and assess risk accordingly.

Nationally, default rates on EE on-bill programs is in the 1% to 2% range. There is no definitive answer as to why the default rate is low. Some program administrators attribute the low default rate to "follow the meter" provisions, others attribute it to the single bill with "payment neutral" provisions, and yet others claim their ability to disconnect is the answer; all of which have been recommended by counsel for pursuit of explicit statutory authorization.

Even though EE on-bill programs have demonstrated low default rates, traditional lenders have yet to recognize this when considering interest rates on EE related loans. This may be due to the fact that EE programs are relatively new to the lending marketplace.

Utility costs associated with administering on-bill programs generally have been shown to be high, about 10% to 15%. These costs are associated with the utility issuing bills, collecting payments, making payments on behalf of customers, etc. In addition to labor costs, costs associated with hardware and software upgrades to the utility billing system can be substantial and should be considered and estimated. Utility program administration costs are born by the customers that use the OBR program. The costs are passed through either by including them in the interest rate (monthly bill) or in the loan application fees.

As a result, costs associated with the loan to the consumer include lender costs and utility costs. Typical third party lender programs have interest rates that include protection against default. IGU is considering several actions to minimize the costs to the consumer of third party capital and also to minimize the risk of default.

Traditional, for-profit lending institution rates may be reduced if the utility is willing to share the risk of default by using utility funds to provide a loan loss reserve or "backstop" to protect the lender from default. This action is used by other utility programs. The Plan contemplates the provision of a backstop to protect against defaults and reduce interest rates, though funding for such a backstop remains undefined.

One of the most common and widely used credit enhancement strategies due to its ease of implementation is the Loan Loss Reserve (LLR). It entails the setting aside of a limited pool of funds from which the financial entity can recover a portion of their losses in the event of borrower defaults. Typically, the size of LLRs are in the range of several percent up to 10% (i.e., the loan pool coverage ratio) of the amount of capital allocated for the program. In this case, the loan pool coverage ratio is the maximum percentage of a pool of loans that can be recovered from the LLR. The lower the loan pool coverage ratio, the higher the leverage of the capital monies (e.g., a 5%, $1 million LLR can support $20 million in lending and leverage LLR monies 20 to 1).

Another typical component in the LLR is the loss-share ratio, which is the percentage of a lender's loss on each default that can be recovered from the LLR. For example, an 80% loss-share ratio would allow a lender or investor to recover 80% of the loss from each loan default in the LLR up to the maximum loan pool coverage ratio. The lender or investor would be absorbing the 20% difference. These LLR terms are typically negotiated between the program administrator and the lender, depending on the program goals, target sector being served and the risk tolerance of the lender. LLR monies are typically placed in an escrow account at the start of the program, and then drawn down if defaults occurs. (Source: EESI "How-to Guide" Launching an On-bill Financing Program, 2016).

2.2 RATEPAYER FUNDS

IGU is evaluating the use of ratepayer or other public funds as a separate, dedicated funding mechanism to support the on-bill repayment program. Theoretically, ratepayer funds could be used to provide loan loss reserve funds or loan interest rate buy-down for consumers.

Whether or not this is possible for IGU is dependent, in addition to availability of internal funds, upon the utility's legal authority to use public funds in this manner. A review has been conducted and is discussed below. In addition to legal consideration regarding the use of public funds, typically there are cost-benefit requirements associated with the use of ratepayer funds by a public utility.

2.3 LEGAL AUTHORITY CONSIDERATIONS

At this time, there is no precedence in Alaska for an on-bill repayment program as suggested by IGU. As a result, it is necessary to determine the extent of legal authority or authorization requirements needed for implementation of certain contemplated program elements, including protection against defaults, which impact the utility customer.

Repayment program elements under consideration and legal review include, but may not be limited to, the following:

- Sponsoring and supporting an on-bill repayment program – which includes collecting loan repayment funds from rate payers and making payments to a third party (lender) on behalf of the consumer.
- Utilizing rate-payer funds or state funds to support a utility-specific financing program:
  - Loan loss reserve/backstop against default (currently perceived to be a loan obligation from the Fairbanks North Star Borough (FNSB) to IGU).
  - IGU administrative fees to support the financing program.
  - Interest rate buy down to achieve an attractive rate.

- Marketing efforts for the financing program.

- Authority to attach consumer loans to property so as to "follow the meter" as a tariff, or other means of transferring the loan payment responsibility should the property be sold.
- Ability of the utility to shut-off service for non-payment of third-party debt.

3.0 IGU ON-BILL REPAYMENT PROGRAM

To support the utility goal of "as many conversions as possible," which translates to "as many new customers as possible," a strong customer-centric program is envisioned for IGU. Administration of an IGU-sponsored customer service program is anticipated to be integrated within the utility's administration and operation policies, practices, and protocols. The addition of a new customer on-boarding program featuring an on-bill repayment offering is an element of the overall utility administration.

3.1 ROLES AND RESPONSIBILITIES

Table 1 depicts the proposed division of responsibilities for the IGU on-bill repayment offering. The responsible entities include those of the utility and also third party participants. This tool is used to manage risk, identify program needs, and facilitate program development. The table was completed with input from the IGU General Manager.

Table 1 On-bill Program Roles and Responsibilities

Work Area	IGU	Third Party	IGU/FNSB
Finance			
Provide and manage program capital		X	
Loan approval and origination		X	
Loan servicing		X	
Provide credit enhancements	X		
Customer Interface			
Marketing	X		
Primary contact for participant	X		
Managing on-bill payments	X		
On-Site Activities			
Contractor recruitment/training/approval	X		
Contractor coordination	X		
Home audits / Energy modeling		X	
Project approval (pre- and post-work)		X	
Other Administration Activities			
Overall program administration	X		
Evaluation, monitoring & verification			X
Legal issues			X

Key:
FNSB – Fairbanks North Star Borough IGU – Interior Gas Utility

3.2 FINANCE

Using third party capital to support conversions relies on lending institutions expertise and mitigates the risk to IGU associated with consumer lending. IGU will work with lenders to understand and, where practical, define loan program attributes for the on-bill program with respect to creditworthiness requirements and potentially interest rate reduction actions. However, the lenders will hold responsibility for providing capital, and issuing and managing the individual loans.

IGU will collect payments and make payments to lender(s) based upon the terms of the loans. This will require the IGU billing system to either have or allow this functionality. This program aspect will be further reviewed when information relative to the existing or proposed billing system for the integrated utility is available.

3.3 CUSTOMER INTERFACE

Review of long-term utilities implementation of on-bill programs revealed that, typically, on-bill programs are added to bolster utility participation and energy efficiency through heating unit and appliance changes. Such utilities have well established administration practices and requisite, in-place staff for on-boarding new customers. When gas is available, it is assumed that IGU will have staff available and policies in place to support utility activities associated with new customer on-boarding. These include:

- Customer service.
- Marketing and communications.
- Billing and account administration.
- Service line installation coordination.
- Heating system functional check-out or other method for system acceptance prior to gasification.
- Legal.

For IGU, it is expected that the addition of an on-bill repayment program will represent a slight increase in staffing above that needed to implement the “one-stop shop” service offering. To implement the on-bill program, IGU will either need to hire or cross-train administrative and operations staff to include the following activities:

- Provide program information to customers, lender(s), and contractors.
- Coordinate with lender(s) and contractors.
- Confirm creditworthiness, if using utility defined metric.
- Confirm installation.
- Include provisions to on-bill customer accounts.
- Implement on-bill partial or non-payment protocol, as appropriate.
- Coordinate payments with lender(s).
- Implement lien/account transfer, if the loan follows the meter.

The financial impact of implementing a “one stop shop” on-boarding strategy with an on-bill program will be estimated when the following are known and taken into consideration:

- The price of gas after 2021.
- Gas availability to IGU.
- Operational structure of the integrated utility.

3.4 ON-SITE ACTIVITIES

On-bill related on-site activities include not only customer coordination, but also coordination with installation contractors. Existing programs with high participation rates report that contractor engagement is central to success. For these programs, utilities work with contractors and provide them with information relative to the financing program so that contractors can inform their customers. Much like auto dealers providing financing to new car buyers, this includes providing contractors with the means to provide customers with loan application and submittal services.

Once approval has been granted, and the installation work has been conducted, the utility representative provides an audit of the installation to ensure the work is complete as bid and is consistent with the terms of the loan. This step is necessary to facilitate contractor payment and service activation.

3.5 OTHER ADMINISTRATIVE ACTIVITIES

There are additional administrative activities associated with on-bill repayment programs which must be addressed by the utility. These include, in addition to overall administration, monitoring program participation metrics and legal involvement. Monitoring program metrics allows the utility to determine the success of the program based upon utility defined expectations. This may include participation rates, default rates, and costs to administer the program. Legal involvement may be required to resolve matters associated with non-payment or default.

4.0 LEGAL AUTHORIZATION

IGU seeks to develop a program that allows customers to participate at the lowest cost possible but also balance risk to the utility. In addition to implementing an on-bill collection/payment mechanism for third-party debt, this includes consideration of implementing the following program terms:

- Terminating service for lack of payment or default.
- Structuring loan to “follow the meter” and not the customer.
- Establishing a loan loss reserve as backstop against default.

As noted, in Alaska there are currently no on-bill programs such as proposed by IGU. And Alaska law is silent regarding a number of mechanisms noted as being major contributors to

programmatic success. This brings into question whether or not IGU has the legal authority to implement an on-bill program and administer it as proposed.

To determine legality, IGU obtained a legal review from CSG, Inc. With reference to the opinion provided, it is recommended that IGU seek to obtain certain explicit authorizations. The complete legal response from CSG, Inc. is provided in **Appendix B**. Further definition of statutory and regulatory needs may also be forthcoming should the Alaska legislature and administration officially request investigation by the Regulatory Commission of Alaska.

Summary examples of authorizing language used by other programs with similar provisions being considered by IGU are provided in **Appendix C**.

It is anticipated that development of authorizing language for approval by the Alaska State Legislature will be inclusive, with participation or input obtained from other Alaska-based utilities. This will result in an action that meets the needs of other utilities, as well as those of IGU. It is anticipated that any action by the Alaska State Legislature will be advanced by IGU with legal support and timely to support the first conversions.

5.0 ON-BILL PROGRAM IMPLEMENTATION SCHEDULE

For planning purposes, Stantec and EESI provided a high level timeline, **Table 2**, for implementation of an on-bill program as proposed by IGU. It should be noted that in order for the program to be implemented, planning and staffing are needed for program development. This includes legal authority and integrated operational plans, policies, and procedures necessary for implementation.

Table 2 High Level On-bill Repayment Program Implementation Timeline

Timeline	Develop
Year 1 – Initial Planning	
Quarter 3	• Set enough key program details so that discussions can begin with lenders.
Quarter 4	• Hold exploratory conversations with financial institutions. • Initiate Request for Information/Request for Proposal processes. • Submit requests for legislative changes.
Year 2 – Further Planning and Program Ramp-Up	
Quarter 1	• Negotiate deal with financial institution, as appropriate. • Legislative changes are approved.
Quarter 2	• Sign agreement with financial institution, as appropriate. • Create pre-launch work plan and assign roles. • Create program delivery process charts explaining roles and responsibilities.
Quarter 3	• Meet with potential contractors and other stakeholders. • Set procedures with financial institution for loan origination and flow of capital.
Quarter 4	• Develop program application and participation agreement. • Recruit additional contractors. • Develop IT implementation plan for on-bill repay.

Year 3 – Gas Delivery and Program Launch	
Jan - Feb	• Develop contractor management plan (including QA/QC process). • Develop marketing plan. • Finalize loan servicing plan with financial institution. • Finalize program administration procedures.
Mar	• Hold pre-launch meetings with contractors. • Finalize web portal and marketing materials.
Apr	• Program launch (pilot phase).
May	• First conversions completed.
June	• Evaluate and modify program procedures.

Key:
QA/QC – Quality Assurance/Quality Control

Table 2 provides an overview of the activities that will need to be in place prior to the first on-bill program customers, which occurs in Year 3.

6.0 CONCLUSION

Based upon the work conducted to date, it appears that the customer service and on-boarding program, including and on-bill repayment offering, is consistent with programs of other utilities seeking to bolster participation. While there are limited examples of gas utilities providing these services for natural gas conversions, the example provided by the Chambersburg PA Municipal Utility operates with similar goals, drivers, and program administration attributes. Funding for an IGU on-bill program will likely focus on leveraging programs offered by existing lenders and third-party capital to make the most of IGU's initially limited internal funding capacity.

Legal review relative to the authority of IGU to implement an on-bill repayment program, reveals additional work in this area is needed. Pursuing explicit authorization will require legislative involvement and action prior to implementation. Development of the authorizing language appropriate for use in Alaska, is expected to include stakeholder engagement from other utilities that may have an interest in implementing an on-bill program.

To determine cost of administration, more is needed relative to the operating plan of the combined utility. Current economic conditions in Alaska are depressed and the price differential between fuel oil and natural gas is low. As a result, consumers may be inclined to delay conversions. Therefore, to attract new customers, it is expected that a strong customer service program will be essential to bolstering and promoting residential conversions. Developing the scope, staffing, and timing for a customer service program with an on-bill repayment option are recommended and planned for future effort.

Appendix A OBF CASE STUDY

Chambersburg, PA Municipal Utility – OBF for Natural Gas Conversions

The Borough of Chambersburg is a municipal utility that provides natural gas, electric, water, trash, and waste services to about 20,000 residents in south central Pennsylvania. Besides Philadelphia, Chambersburg is the only municipality in the state that owns and operates its own natural gas utility. It is also one of the few municipal gas utilities in the country offering a financing program to convert homes to natural gas. Participating customers repay the loan to the city over time as part of their utility bill, making this an on-bill financing program.

Program Overview

The Borough of Chambersburg's Natural Gas Department launched the "Main Street Energy Efficiency Financing Program" in 2011. In the past six years, the program has helped convert approximately 400 homes from heating oil to natural gas. The program has loaned out $1.75 million to participants, with individual loans capped at $5,000.

All participants in the conversion program are already members of the broader Chambersburg municipal utility. At the program's outset, approximately one half of the city's 10,000 utility customers used natural gas for heating. The utility developed the conversion on-bill financing program to increase the share of customers using gas (and thus grow its revenue base). Additional goals of the program are to deliver energy cost savings to city residents, bolster local contractors, and improve the environment by reducing fuel oil use. Chambersburg utilities are not regulated, so authorization was not needed from the state for this program. Rather, the borough council voted to approve the program.

While the program is administered by the Chambersburg municipal utility, the loan capital comes from the Municipal Gas Association of Georgia (MGAG), of which Chambersburg is a member. (The peculiar geography of this is partially explained by there being only two municipal gas utilities in Pennsylvania.) MGAG provides Chambersburg with an interest-free credit line of $5 million, along with some administrative support. Chambersburg then serves as pass-through for the loan repayments to MGAG.

Measures and Savings

The conversion program provides loans to customers to remove fuel heating equipment and replace it with high-efficiency gas furnaces and tank-less gas water heaters. The average Chambersburg natural gas customer spends $550 per year, and the utility estimates that to be a $1,550 per year savings over heating oil. Assuming a conversion cost of $5,000 with minimal financing costs, the average project has a simple payback of less than 3.5 years. But because a project loan is for five years, participants save an average of $500 per year in total energy costs even while repaying the loan.

Local Fuel Costs in Chambersburg

Natural Gas: $0.58/ccf = $5.62/MBtu

Heating Oil #2: $2.65/gallon= $19.13/MBtu

Heating oil costs 3.4x more than natural gas

For quality assurance, the utility inspects the completed work on every participating home. The utility must sign off on the work in order for contractors to be paid. The utility reports that it has a good relationship with the local contractor network, which has benefited from the additional business.

Financing

Loans for the program are capped at $5,000, to be repaid over five years. The utility charges zero percent on the loans, but adds a $3 per month administration fee on each loan. Therefore, a customer that needs a max loan and uses the full five-year repayment period will pay $86 per month (not including any fuel savings). The loan payments are included as a line item on the customer's combined municipal utility bill. To be eligible, homeowners must already be a customer with other Chambersburg utility services and have two years of good utility bill payment history. No additional credit check is performed. The loans have been low-risk for the utility, with only one default in the first six years of the program. The loans are attached to the individual and not the meter, which means that the loans cannot be transferred to the next occupant of the home.

Administrative Details

The Chambersburg utility operates the conversion loan program with few overhead costs. The utility relies on the local contractor network and word-of-mouth to market the program. The utility did not add staff to run the program, but instead relies on existing personnel to approve applications, coordinate with contractors and participants, and handle loan collection. The utility reports that this has not added significant burden to staff, though it does rely on MGAG staff for certain tasks. MGAG provides centralized support and loan capital for 19 municipal utilities' energy efficiency financing programs, mostly in Georgia, but Chambersburg is the only one to offer financing for natural gas conversions.

Future

The Borough of Chambersburg is pleased with the results and will continue to offer the program for the foreseeable future. It has more than $3 million in loan capital available through MGAG, with the possibility of increasing the pool and/or converting it to a revolving loan fund. Recently, Chambersburg expanded the program to include small commercial customers. The first commercial loan was completed in mid-2017.

Notes: Q&A with John Leary, head of the Chambersburg Gas Department

1) Are the conversions related to existing utility customers or new customers?

   A: All conversions are for people that already use Chambersburg Borough utilities. Most are for those customers that previously didn't have gas, but we do also have some for people who had gas but used something else as their primary heating fuel.

2) If existing customers, is your utility a gas/electric combination which allows you access to customer utility bill payment history?

   A: Yes, we are a combo utility (gas/electric/water/sewer/trash), so we do have access to their utility bill payment history.

3) If new customers, what is your qualification process, does it change? Again the question of access to payment history comes up.

A: Any "new customers" are just new to gas, so we still have their payment history for the other Chambersburg utilities.

4) Please remind me of your total potential new customer pool, and number of new conversion customers per year with financing and without.

A: We have about 21,000 residents, or about 10,000 households/business unit. We have about 5,850 gas customers. We have been adding about 75 gas customers per year, with about 50 of those due to the financing program.

5) If a customer doesn't utilize the on-bill program, do the utility supported quality and contractor programs change? Or do all new conversions customers go through the same on-boarding process regardless of funding source?

A: I'm not sure if I understand this question, but will still try to answer it...if I don't, please let me know what I'm missing! We have the same gas piping safety requirements for all new gas work, whether done through the Financing Program or not. We don't have the quality control portion of requiring the customer is happy with the installation/work of the contractor if not done under the loan program - we only make sure the work is done safely and per code.

6) We are trying to get an idea of the number of our potential new customers that will take advantage of an on-bill program versus those that would use savings or other means to pay. In this context, if you can – what percentage of your total pool uses personally obtained funds for conversion and what percentage the on-bill repay program?

A: This is an item I'll have to give a rough estimate on based on anecdotal evidence, but I'd say probably 2/3 to 3/4 utilize the financing program, with 1/4 to 1/3 paying out of pocket.

7) Regarding price differential between fuel oil and natural gas, have you determined a cost point where the energy cost savings differential is not significant enough to promote conversions?

A: Almost all people would prefer to use natural gas over heating oil, given the choice (due to cleaner smell in the home, cleaner burning for the environment, better reliability - especially during snowstorms or extreme cold, better convenience - no longer having to have tank re-filled, as well as of course cost). But if people didn't save money - or at least break-even, most wouldn't convert. To give a good answer, I'll show this general analysis:

- Assume people would want a financial break-even within ten years to decide on the conversion
- Heating oil retail price of $2.65 per gallon; Henry Hub natural gas price of $2.80; Chambersburg retail price approximately $0.58 per CCF
- Average annual bill for gas customer $555. Since the conversion of gas @ 1,000 BTU/ft3 and #2 oil @ 138,500 BTU/gal yields a multiple of oil cost vs. gas cost of 3.786, multiplying $555 by 3.786 yields an average annual bill for a heating oil customer of $2,100
- Annual savings with gas: $2,100 - $555 = $1,545
- Assume conversion cost = $5,000
- 10 year savings = (10 x $1,545) - $5,000 = $10,450: To look at 5 year savings: (5 x $1,545) - $5,000 = $2,725
- To have 10 years be the break-even mark, I'll go backwards: 0 (break-even) = (10 yrs x X savings) - $5,000 cost

- This calculates to X = $500 per year energy savings
- To only get $500 per year in energy savings with gas vs. heating oil, the price of natural gas would have to rise by a factor of $1,545/$500 = 3.09, or the price of heating oil would have to decrease by the factor of 3.09. This would mean that our retail price of $0.58 per CCF would have to increase to $1.79 per CCF - which would require a Henry Hub gas price of approximately $14 per MMBTU....or the price of #2 heating oil would have to fall to approximately $2.65/3.09 = $0.86 per gallon.

8) What is your quality assurance process for the conversions? If you do post-install inspections, do you reduce the frequency for contractors that have proven to do quality work?

A: We inspect every install to verify the units and piping are working and done properly - no matter who does the work.

9) How would you characterize your relationship with the contractors?

A: We mostly have a great relationship with the contractors. They love the extra business. We allow out of town contractors to do the work, and sometimes get in fights with them when they try to circumvent the rules or do shoddy work, but I can live with that!

10) Why do you have this program? On-bill financing programs for conversions are very rare. Is it a primarily a growth strategy?

A: We do have the program primarily as a growth strategy. It is also a large benefit to our residents (who we exist to serve), and a good economic growth engine.

11) What were your growing pains over the first year or so? What advice to give a program still in the design phase? Growing pains were less than I expected.

A: The biggest issue in getting started was getting people to start using it. That didn't take long, but publicity and advertising are not our strongest suit. Once neighbors and contractors got started though, the word spread without our efforts and the program greatly expanded.

12) Did you need to convince your board to approve financing for conversions? What was the winning argument?

A: Yes, we did have to get their approval. But it was an easy sell. There is very small financial risk, but a large benefit in expanding the customer base. I think the important "arguments" are growing the customer (i.e. revenue) base, helping residents see a large financial savings, helping out local businesses, and benefiting the environment by replacing dirtier heating sources with clean natural gas.

13) What is the process for adding loan payments to the bill and tracking pay back? Does it integrate with your billing software?

A; Our Finance Dept. has a program (QuikCalc) for tracking loans. I complete a spreadsheet with each new loan to provide to Finance. I have attached that spreadsheet (with names and accounts removed). Finance has been able to add a line item to the billing software for the loan repayments, which then requires little to no manual follow-up on their part once inputted.

14) What is your application/approval process? You mentioned that it was a relatively low burden for you -- we're very interested in trying to replicate that for other program managers. (The MGAG support staff helps in that regard, I imagine.)

A: I have attached a copy of the loan application. It was initially created by MGAG, and I have modified it slightly to personalize it for Chambersburg. MGAG isn't involved in the approval process unless I have questions. I know they wouldn't mind helping more, but it's simple enough I don't need any assistance. Once I receive the application, I pull up the customer's billing history. That history is immediately available on my desktop, and lets me quickly verify their utility bill payments back two years, as well as verifying they are the owner of record for the property. I could easily have my secretary or someone else do this, but it takes very little time. I then pull up a quick form letter and have my secretary update for the person and send out.

15) Among on-bill programs, it is rare to approve applicants using bill payment history AND to use personal loans (rather than meter-attached). Personal loans are typically approved using a credit score. Why do you decide to do it this way? Or was this design set by MGAG?

A: MGAG set up the program to have approvals either by payment history or credit score. Payment history is (I believe) much easier and quicker for me to check so I went with that. I suppose credit history may be even quicker and easier, but I'm not familiar with checking that for anyone other than my own so I don't have a real familiarity with it. Utility bill payment history has been for us a good predictor of loan repayment reliability, so I'm happy with the way it works.

16) This one is tough, but could you speculate on how a higher monthly fee or interest rate would impact program participation? Do you have anecdotal evidence that people are going for it more because of convenience or the low-cost capital?

A: Yes, good question. I think people love to hear "0% interest", so that really does help sell the program. But I believe most people would recognize the benefits anyway, and would still participate even with higher fees or rates. When people pay $3,000 or $4,000 a year for heating oil, and see that they could pay less than $1,000 a year with natural gas, they tend to get real excited to switch. Paying $1,000 a year in loan repayments is understood as an OK investment to save $2,000 or $3,000. I would think that higher fees/rates, even say to make the repayment $1,500 a year, would still be seen as a positive. To answer your question, I have seen both reasons - some people like the convenience, other the low cost...everyone likes having their upfront out of pocket costs eliminated.

Appendix B LEGAL REVIEW

CSG, Inc.

Attorneys at Law

Barbara L. Schuhmann - of Counsel
Robert B. Groseclose
Jo A. Kuchle
Zane D. Wilson
Craig B. Partyka
Danielle M. Gardner
Ehren D. Lohse
Kristina M. Miller

Telephone 907.452.1855 • Facsimile 907.452.8154 • Toll Free 800.550.1855
714 Fourth Avenue, Suite 200 • Fairbanks, Alaska 99701-4470
www.alaskalaw.com • csg@alaskalaw.com

August 2, 2017

sender's email address:
reneb@alaskalaw.com

Jomo Stewart
Interior Alaska Natural Gas Utility
PO Box 70200
Fairbanks, Alaska 99707

Re: Proposed On-bill Repayment Program
Our File No. 6535.01

Dear Jomo:

You asked several questions concerning the legality of a proposed on-bill repayment program that would, using your term, "follow the meter" as opposed to the borrower. As I understand it a third-party lender would actually make the loan to the consumer but IGU would administer the program and protect lenders from borrower default by terminating or suspending IGU service for nonpayment and through an IGU loan loss reserve from which the third-party lender would get paid if the borrower defaults.

This proposal raises a number of legal issues which are disclosed at length below.

Can IGU legally establish a loan loss reserve and make payments upon borrower default?

Maybe depending on the funding source for the loan loss reserve. There are at least three issues of concern that may arise depending on the funding source.

First, IGU is a municipal utility essentially owned by the Fairbanks North Star Borough taxpayers. Accordingly, IGU's money is public money. Alaska's Constitution allows the use of public money and public credit only for a public purpose.[1] Here public money, upon default by a borrower, would be used to pay private debt. There, however, may be a strong argument that a public purpose exists due to the positive impact the loan program may have on air quality and increasing the customer base thereby lowering the cost of gas to all customers.[2] To the extent IGU decides to fund a loan loss reserve it

[1] "No tax shall be levied, or appropriation of public money made, or public property transferred, nor shall the public credit be used, except for a public purpose." Art. 9 §6.

[2] Austin Energy in 2015 declined to adopt an on-bill financing program of energy efficiency improvements finding that "Austin Energy's role as surety in guaranteeing repayment of a loan through utility billing and through the established recourse for nonpayment (e.g. disconnection of utility service) may violate the Constitutional prohibition of a municipality lending credit in support of the debts of private persons." (Copy attached).

should carefully document and establish the public purpose of the reserve's use to pay private debt.

Second, IGU cannot promise or make any guarantee of payment beyond its available funds, i.e. its reserves or revenue of the utility. Any guarantee beyond that would constitute unconstitutional debt.

Third, a strong argument could be made that a loan loss reserve funded by mandatory charges to utility customers regardless of whether they benefit from the service creating the cost constitutes an illegal tax.[3] The United States Supreme Court has defined a tax as an "enforced contribution to provide for the support of government."[4] In contrast, a "fee . . . is incident to a voluntary act . . . which, presumably, bestows a benefit on the applicant, not shared by other members of society"[5] Thus, when a government entity charges its citizens, the charge will generally only be considered a fee rather than a tax if it is directly connected to the cost of a service that citizen may choose or decline, e.g. a user fee that can at the option of the customer be avoided.[6] The cost of paying for a borrower's default and administering a loan program at best could probably only be charged to all loan recipients as opposed to charging a customer who does not directly benefit from the loan program.

Can IGU legally place the loan repayment charges on a customer's utility bill?

Yes, pursuant to a written contractual agreement, but it would be safer to have explicit legal authority authorizing this charge particularly if IGU plans on disconnecting the utility service for nonpayment. There does not currently appear to be a state law prohibiting a municipal gas utility from placing loan repayment charges on a customer's utility bill. As a publicly owned utility, IGU largely remains unregulated and exempt from most RCA regulations. It would be preferable, however, to have explicit legal authority to place these charges on a customer bill as historically utilities have generally not possessed the authority to put third-party debt on a utility bill.

If IGU places the loan repayment charges on a customer's utility bill, can IGU legally suspend or terminate service for lack of payment?

Technically yes. IGU, as discussed above, is largely unregulated by the RCA and there is no existing state law or regulation prohibiting disconnection of gas. However, given

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[3] See, e.g., *Harbor Village Apartments v. City of Mukilteo*, 139 Wash. 2d 604, 989 P.2d 542 (1999)(Invalidating as an illegal property tax a residential dwelling unit fee charged to every rental unit regardless of whether it was actually rented and thus a rental property owner could not avoid the "fee").
[4] *United States v. Mississippi Tax Comm'n*, 421 U.S. 599, 606, 95 S.Ct. 1872, 44 L.Ed.2d 404 (1975).
[5] *National Cable Television Assn. v. United States*, 415 U.S. 336, 340-41, 94 S.Ct. 1146, 39 L.Ed.2d 370 (1974).
[6] Generally, courts look at (1) the primary purpose of the fee (2) whether the money is allocated solely to the authorized purpose and (3) whether there is "a direct relationship between the fee charged and the service received by those who pay the fee or between the fee charged and the burden produced by the fee payer." *Covell v. City of Seattle*, 127 Wash 2nd 874, 879 904 P.2d 324, 327 (Wash. 1995).

the potential litigation that may arise from suspension or termination of service, it would be much safer to have explicit legal authorization to suspend or terminate service--particularly if gas is the only heating source for the building.[7] Paradoxically, suspension or termination of service for non-payment will be an ineffective remedy for customers with alternative heating sources. It probably goes without saying that any suspension or disconnection in the winter may, even if legal, generate potential lawsuits or public condemnation particularly when the service is cut off in order to force payment on a third-party debt.

Can/Should the loan be structured to "follow the meter" and not the customer?

Yes, it can be structured to follow the meter through a contractual obligation with notice and required assumption or payoff by purchasers, but this structure will create fairly significant administrative, recording and collection costs. You may want to have the option of both—in other words, make the customer personally liable with the additional right to either collect from future purchasers through assumption of the obligation or payoff and by placement of a lien on the real property.

Sincerely,

CSG, Inc.

By: _____
A. René Broker

Enclosures
Cc: Monique Garbowicz (Monique.garbowicz@stantec.com)

[7] RCA heavily regulates disconnection of electric service apparently due to the life, health and safety issues associated with electric service including requiring additional notice and delay when the utility is disconnecting a residence occupied by a person seriously ill, elderly, with a disability or dependent on life support systems. 3 AAC 52.450(c)(2).

Alaska Administrative Code
Title 3. Commerce, Community, and Economic Development
Part 7. Regulatory Commission of Alaska
Chapter 52. Operation of Public Utilities
Article 5. Electric Utilities

Current through July 22, 2017

§ 3 AAC 52.450. Disconnection of service

(a) A utility may disconnect service to a customer without advance written notice under the following conditions:

(1) an immediate hazard exists which threatens the safety or health of the customer or the general population or the utility's personnel or facilities;

(2) the utility has evidence of meter tampering or fraud by the customer; or

(3) a customer has failed to comply with the curtailment procedures imposed by a utility during emergency supply shortages.

(b) A utility may commence disconnection procedures in accordance with the notice requirements of (c) of this section for any of the following reasons:

(1) failure of the customer to pay for utility service within 40 days after initial rendering of the bill unless the customer has entered into a deferred payment agreement;

(2) failure of the customer to meet or maintain the utility's deposit requirements;

(3) knowing and continued failure of the customer to provide the utility with reasonable access to its meter, equipment, or property;

(4) customer breach of a special contract between the utility and customer for utility service; or

(5) necessity of the utility to comply with an order or regulation of any governmental agency with proper jurisdiction.

(c) The following notice requirements apply to service disconnections permissible under (b) of this section:

(1) Except as provided in (2) of this subsection and in (d) of this section, a utility shall, at least 15 days before the scheduled date of disconnection, mail or deliver to the customer a written notice of its intent to disconnect service. A copy of the termination notice must be simultaneously forwarded to any third party designated by the customer on a service application. The notice must contain, at a minimum, the following information:

(A) the name and address of the customer whose service is to be disconnected and the service address, if different;

(B) the date on or after which service will be disconnected unless the customer takes appropriate action;

(C) an explanation of the reason for the proposed disconnection, including, if appropriate, a statement of the amount of the delinquent bill which the customer has failed to pay in accordance with the payment policy of the utility;

(D) if disconnection is premised on payment delinquency,

(i) a statement advising the customer to contact the utility for information regarding deferred payment and other procedures that the utility may offer to avoid disconnection of the customer's service; and

customer's service, and

(ii) a list of any governmental or social assistance agencies, of which the utility is aware, that may offer energy assistance to qualified needy customers;

(E) a specific request that if a customer's residence is occupied by a person seriously ill, elderly, with a disability, or dependent on life support systems, the customer should notify the utility immediately of that circumstance for consideration in avoiding disconnection;

(F) a statement advising the customer that the utility's stated reason for the termination of service may be disputed and potentially resolved by contacting the utility at a specific address or telephone number;

(G) a statement that the utility retains the right to terminate service, after allowing a customer who disputes a bill the opportunity for a meeting, if the utility continues to find that the reason for the disconnection is just;

(H) the telephone number and mailing address of the commission, the Internet address of the commission's website, and a statement that the customer may file a complaint with the commission under 3 AAC 48.120 or 3 AAC 48.130 if not satisfied with the utility's response or resolution of a contested bill or tariff provision; and

(I) the amount of the utility's tariffed charges for disconnection and reconnection of service.

(2) If a utility has been informed that a residence is occupied by a person seriously ill, elderly, with a disability, or dependent on life support systems, the utility shall provide the notice required by (1) of this subsection at least 30 days before the scheduled date of disconnection. In any case in which a utility is notified after issuance of a termination notice that a customer's residence is occupied by a person seriously ill, elderly, with a disability, or dependent on life support systems, the utility shall extend the disconnection date by 15 days and notify the customer of the extension.

(3) Not less than three working days prior to disconnection, the utility shall attempt personal contact with the customer either by telephone or by visit of an authorized utility representative to the premises. If by telephone, the utility shall attempt to make contact no less than three times at various periods in the day or make other reasonable attempts to contact the customer. A utility shall keep records of all attempted and completed telephone contacts, showing at least the time, the person making the attempt, and the outcome. If by visit to the premises, the utility's authorized representative shall hand-deliver a "Shut-Off Notice" to the customer or, if no personal contact is possible, leave the notice in a prominent place. If the premises is 25 or more miles from the nearest location from which the utility delivers notices and if telephone contact cannot be made, a first class, postage-prepaid letter may serve as an alternative to a hand-delivered "Shut-Off" notice. This notice must be mailed no less than five working days before the date scheduled for disconnection. The "Shut-Off Notice" or completed telephone call must provide the customer with the following information:

(A) the name and address of the customer and the service address, if different;

(B) a concise statement of the reasons for the impending disconnection of service;

(C) the date on or after which service will be disconnected;

(D) the business office telephone number, after-business-hours telephone number if applicable, and the address of the utility where the customer may pay the delinquent bill, enter into a deferred payment agreement, or file a bill dispute complaint; and

(E) the amount of the charges for disconnection and reconnection of service.

(4) If a utility knows that a landlord/tenant relationship exists, the following additional provisions apply:

(A) For individually metered premises where the landlord is the customer, the utility shall notify the tenant in writing, at least 15 days before the scheduled date for disconnection of the service to the landlord, of the option of subscribing for service in the tenant's own name. However, the utility may not attempt to recover from the tenant or condition service to the tenant on the payment of any outstanding bills or other charges due from the outstanding account of the landlord. If, however, the tenant has a previously outstanding balance at the same service address, the utility may condition service to that tenant on terms acceptable to the utility for repayment of the outstanding balance plus a deposit in compliance with the utility's tariff. If the tenant declines to subscribe for individual service, or arrange for payment of the tenant's outstanding balance, if applicable, the utility may disconnect service without further notice, no earlier than the date scheduled for disconnection.

(B) For master-metered premises where the landlord is the customer, the utility

(B) for master-metered premises where the landlord is the customer, the utility

(i) after the expiration of the notice period provided in (1) - (3) of this subsection, shall additionally provide individual notice of the pending disconnection to each tenant served through the master meter at least 14 days before disconnection; or

(ii) at least 15 days before the scheduled date of disconnection of the landlord, shall give each tenant served through the master meter notice of the pending disconnection.

(C) If the tenant is the customer, the utility shall notify the landlord in writing, at least 15 days before the scheduled date of disconnect of the tenant, of the option of subscribing for the service provided at the tenant's premises. However, the utility may not attempt to recover from the landlord or condition service to the landlord on the payment of any outstanding bills or other charges due from the outstanding account of the tenant. If, however, the landlord has a previous outstanding balance at the same service address, the utility may condition service to that landlord on terms acceptable to the utility for repayment of the outstanding balance plus a deposit in compliance with the utility's tariff. If the landlord declines to subscribe for service or arrange for payment of the landlord's outstanding balance, if applicable, the utility may disconnect service without further notice.

(d) At least three working days before disconnection, a utility shall give written or telephone notice of disconnection, in accordance with (c)(3) of this section to a customer who has failed to comply with a deferred payment agreement.

(e) Within 10 days after the date specified on a "Shut-Off Notice", a utility may, without further notice, disconnect service to a customer between the daily business hours of 8:00 a.m. on Monday to 5:00 p.m. on Thursday. Service may not be disconnected on a Friday or a day preceding a holiday.

(f) A utility may not disconnect service to a customer for any of the following reasons:

(1) delinquency in payment for services rendered to a prior customer at the premises where service is being provided, except in the instance where the prior customer continues to reside on the premises;

(2) failure of the customer to pay for services or equipment not regulated by the commission;

(3) nonpayment of a bill related to another class of service at a different service location;

(4) the customer disputes the amount due on the delinquent account, complies with the utility's tariffed rules on customer bill disputes, and the dispute remains under investigation by the utility or by the commission; however, a customer shall pay any undisputed amount, and the utility may proceed to disconnect service in accordance with this section for failure to pay any undisputed amounts; or

(5) the customer is unable to pay the full delinquent amount due, qualifies under the utility's tariffed eligibility requirements for deferred payment agreements, and is in compliance with a signed, or is in the process of timely negotiating a, deferred payment agreement.

(g) A utility may remove any or all of its property installed on a customer's premises upon disconnection of service.

(h) A utility shall restore service within three working days after correction of the conditions that resulted in the disconnection. Correction includes execution of a deferred payment agreement. If service is restored during a period other than regular working hours at the customer's request, the utility may impose an after-hours charge for reconnection.

(i) Each utility shall maintain a record of each disconnection of service, including the reason for the disconnection. This record must be maintained for two years and must be available for commission inspection.

Cite as 3 AAC 52.450

History. Eff. 1/1/87, Register 100; am 4/10/92, Register 122; am 11/6/2016, Register 220, January 2017

Editor's Note:

With Register 179, October 2006 and under the authority of AS 44.62.125, the regulations attorney changed obsolete terminology concerning persons with disabilities in conformity with ch. 25, SLA 2006.

Note:

Authority: AS 42.05.141

AUSTIN ENERGY®

MEMORANDUM

TO: Low Income Consumer Advisory Task Force

FROM: Liz Jambor, Manager, DABI

DATE: 02/06/15

SUBJECT: On-Bill Financing

Overview

On-bill financing is a mechanism that allows utility customers to pay for energy efficiency improvements without upfront costs. Through on-bill financing, a utility customer receives a loan to finance energy efficiency improvements and repays the loan on the monthly utility bill. The energy cost savings resulting from improvements offset the cost of the loan repayment, ideally leading to no change to the customer's total monthly bill. Repayment is attached to a property, not to a customer, ensuring that the beneficiary of the improvements is responsible for loan repayment. If a customer moves, the new tenant would assume repayment of the loan.

Several years ago, Austin Energy analyzed the viability of an on-bill financing pilot program in order to achieve greater energy efficiency savings. Several practical impediments arose, and, after discussions with legal staff, it appeared that on-bill financing presented legal issues, including but not limited to the following:

- The Texas Constitution restricts a municipality from lending public credit and providing public money to private parties. As the administrator of loan repayment through utility bills, is Austin Energy assuming the role of surety/guarantor and thus lending its credit to a private entity?
- Does AE have the legal authority to place non-utility charges on the customer utility bill?
- Does AE have the legal authority to disconnect utility service for nonpayment of the loan repayment fee?

Lending of Public Credit

The Texas Constitution prohibits governmental entities from donating or lending public funds and from lending credit in support of the debts of private entities. Under an outside-funded on-bill financing pilot program, the City of Austin would not be providing any public funds for loans to a private entity – a bank would provide the loan funds. The issue is whether the prohibition on a municipality lending its credit applies to Austin Energy's role as the administrator of the loan repayment.

In an Environmental Defense Fund report (Legal Authority of the Public Utility Commission of Texas to Approve A Tariffed Installation Program for Energy Efficiency Measures), Daniel Rosenblum states:

"Lenders are willing to provide funding, since repayment streams are protected by utilities' ability to disconnect for nonpayment of bills, utilities' guarantee of payment and utilities' treatment of nonpayments the same as any other uncollectible (i.e., recovered from all ratepayers)."

Using this analysis of the utility's role in administering the program and assuring debt repayment, Austin Energy would serve in the role of surety and assumes secondary liability for the debt. This would make the program impermissible under Texas law.

A loan of public credit refers to the assumption of some kind of financial liability (both primary and secondary) by the government. The assumption of a financial liability by the government may constitute a loan of credit or may implicate other constitutional or statutory prohibitions. Austin Energy's role as surety in guaranteeing repayment of a loan through utility billing and through the established recourse for nonpayment (e.g., disconnection of utility service) may violate the Constitutional prohibition of a municipality lending credit in support of the debts of private persons.

Non-Utility Charges on a Utility Bill

An on-bill financing program hinges on a utility's authority to include a non-utility charge on a utility bill and to disconnect utility customers for nonpayment of the loan repayment charge. As a home rule city, the City of Austin may charge fees not specifically prohibited by state law, subject to certain legal requirements. Fees not specifically authorized in state law that are in excess of the cost to regulate an activity are an illegal tax. In this case, aside from administration, there is no cost to Austin Energy in providing the service, and Austin Energy would be billing for and collecting the loan repayment fee merely as an intermediary. As a result, the loan repayment fee could be perceived as a cost above Austin Energy's cost and labeled an illegal tax. Therefore, the safest approach may be to wait for affirmative statutory authority to place a third party's debt obligation on utility bills.

pay costs regarding of service

Disconnection for Nonpayment

Another key element in the implementation of on-bill financing programs is the use of utility disconnection as the mechanism for ensuring repayment of the loan. Lenders are attracted to on-bill financing programs by a utility's ability to secure the loan through the threat of disconnection for nonpayment of utility bills including loan repayment fees. However, under the Public Utility Commission rules, electric utility service may not be disconnected for failure to pay for merchandise or charges for non-electric utility service provided by the electric utility. Further, the Austin City Code's Utility Service Regulations do not include non-utility services under a customer's service contract obligations and do not authorize termination of utility service for nonpayment of unrelated City charges and fees. The City's practices regarding termination of utility services for nonpayment of the customer's utility bill are compatible with PUC rules.

Conclusion

The prospect of on-bill financing with Austin Energy and the City of Austin as participants does not appear to be a viable method for financing energy efficiency measures at this time. Due to prohibitions as outlined in the Texas Constitution and the PUC rules, the electric utility cannot serve the role necessary for an effective on-bill financing program to succeed.

An alternative to on-bill financing could be the current loan program through Velocity Credit Union. Velocity currently offers low APR loans to finance energy saving home improvements as well as solar water heaters. These are most often utilized by our Home Performance with Energy Star customers.

Fee or Illegal Tax? Calif. Justices Will Decide Electric Case

MARIA DINZEO April 5, 2017

SAN FRANCISCO (CN) – Southern California Edison customers shouldn't have to foot the bill for a 1 percent electricity surcharge that is actually an illegal tax, a lawyer for a local Santa Barbara hotelier told the California Supreme Court.

l Heidenreich, an attorney who represents Hotel Santa Barbara owner Rolland Jacks on alf of a class of Santa Barbara ratepayers, told the state's highest court Tuesday that the 1 ent surcharge violates Proposition 218 – a voter-passed law that prohibits local rnments from imposing taxes without voter consent.

"Proposition 218 was enacted to expressly limit the taxing powers of local government, and my clients have had financial burdens imposed upon them," he said.

As part of a deal the city of Santa Barbara negotiated in 1999 with Southern California Edison, the utility agreed to pay a 1 percent franchise fee to use city property to deliver electricity. The city then passed an ordinance allowing Edison to pass the surcharge on to customers and send the money to Santa Barbara's general fund.

The surcharge was expected to generate $600,000 in annual revenue and increase monthly electric bills for the average customer by roughly 54 cents.

Jacks brought a class action against the city in 2011, claiming the surcharge is an unlawful tax imposed without voter approval. The city argued the surcharge was just part of the franchise fee agreement.

A state court judge sided with the city, finding the surcharge doesn't qualify as a tax under Proposition 218. An appellate court reversed that decision.

"The 1 percent franchise fee resembles a traditional franchise fee. Its purpose is to compensate the city for allowing Southern California Edison a right-of-way to purvey electricity. The 1 percent surcharge is something else entirely. Its purpose was 'to raise franchise fee revenues for use by the City Council for general city governmental purposes,'" Second Appellate District Judge Steven Perren wrote in reversing the trial court.

On appeal before the state Supreme Court, Heidenreich said the franchise fee, as the city calls it, is very similar to a tax that Edison's customers never agreed to pay.

"My clients are paying a charge. Someone is reaching into their pocket and taking their money, and that someone is the city of Santa Barbara and they did it by enacting Ordinance 5135," he said.

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Chief Justice Tani Cantil-Sakauye challenged Heidenreich's continued reference to the surcharge as a "tax," rather than a "franchise fee," saying that was the crux of the case.

"You keep insisting it's a tax, but that's what we're trying to determine," she said.

Heidenreich said because it was imposed by the city, the surcharge by its very definition must be a tax.

"If it's a direct obligation imposed upon them by the city it cannot be a franchise fee as a definitional matter," he said.

He distinguished the case from *Sinclair Paint v. State Board of Equalization*, where the state's high court ruled that a fee imposed on manufacturers of lead paint is not a tax because the fee was used to pay for health screenings for victims of lead poisoning.

re there is no benefit to my clients," Heidenreich said.

resenting Santa Barbara, attorney Michael Colantuono said the ratepayers do get ething out of the deal.

ey are getting electricity," he said. "We've been allowing people to use public property for private profit, then requiring them to share some of that profit since the beginning of the Republic. I'm advocating that a fee in exchange in consideration for private use of public property is for that reason alone not a tax."

Cantil-Sakauye questioned Colantuono on the benefit conferred by the charge.

"Since 1978, courts have been suspicious about fees masquerading as taxes," she said. "What we've seen is that the fee has to be reasonably related to the value of the service or benefit conferred. In this case, do we know that?"

Colantuono acknowledged this isn't his favorite line of inquiry, but said, "Edison agreed to it and the Public Utility Commission allowed it to be charged to customers and no one on the Santa Barbara City Council got recalled."

His words drew a retort from Justice Carol Corrigan.

"There's a test," she joked.

Colantuono likened the surcharge to a fee for service.

"Let's say we've got office space for rent at City Hall and I'm going to rent a street-facing suite to a travel agency, and I'm going to charge rent to that travel agent. And if the travel agent is a capitalist, and one hopes they are, they're going to recover that rent from their fees for service. You can't have a test which makes that rental payment a tax," he said.

The justices did not indicate how they would rule, which will happen in the next 90 days.

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Taxes vs. Fees: A Curious Confusion

Hugh D. Spitzer*

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*. Affiliate Professor, University of Washington School of Law. Mr. Spitzer practices public finance law with Foster Pepper & Shefelman PLLC, in Seattle, Washington. The views expressed in this Article are solely the author's and do not reflect the position of any client of his law firm.

I. INTRODUCTION

In recent years, local governments have been called upon to provide an increasingly broader range of services and regulatory activities.[1] Those governments have constantly searched for ways to finance the demands placed on them through tax increases,[2] user fees,[3] and other types of charges.[4]

As detailed in this Article, there are constitutional and other restraints on how taxes and fees are structured and applied.[5] In Washington, the distinction between taxes and fees can be decisive in determining whether a particular governmental charge will sustain judicial scrutiny.[6] Unfortunately, Washington case law concerning the distinction between taxes and fees has been murky and confusing, primarily because the courts often resort to a simplistic dichotomy between taxes and regulatory fees.[7] This distinction fails to recognize the existence of alternative charges.[8]

In its 1995 decision, *Covell v. City of Seattle*, the Supreme Court of Washington attempted to provide an updated framework for addressing the difference between taxes and fees.[9] The *Covell* tests, as they came to be known, provided a useful and significant contribution to understanding what actually makes a tax a tax and what makes a user fee a user fee. Notwithstanding *Covell*, Washington courts have clung to the doctrine that every governmental charge can be understood as either a tax or a regulatory fee. Accordingly, Washington courts have failed to adequately acknowledge a different category of fees that was implicitly recognized in *Covell*: *user fees*, including commodity charges and burden-offset charges.[10]

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1. *See generally* 1 A HISTORY OF WASHINGTON'S LOCAL GOVERNMENTS: FINAL REPORT OF THE WASHINGTON STATE LOCAL GOVERNMENT STUDY COMMISSION 29-41 (1988).

2. Franks & Son, Inc. v. State, 136 Wash. 2d 737, 750, 966 P.2d 1232, 1239 (1998) ("A tax is defined as a levy made for the purpose of raising revenue for a general governmental purpose.").

3. *Id.* ("[A] fee is enacted principally as an integral part of the regulation of an activity and to cover the cost of regulation.").

4. *See generally* Mun. RESEARCH & SERV. CTR. OF WASH., A REVENUE GUIDE FOR WASHINGTON CITIES AND TOWNS 41-43 (1999) [hereinafter REVENUE GUIDE].

5. *See, e.g.*, WASH. CONST. art VII, § 2 ("[T]he aggregate of all tax levies upon real and personal property by the state . . . shall not in any year exceed one percent of the true and fair value of such property in money . . ..").

6. *E.g.*, Thurston County Rental Owners Ass'n v. Thurston County, 85 Wash. App. 171, 178, 931 P.2d 208, 212 (1997) ("[W]hether the County has the authority to impose the disputed fees depends upon whether they are taxes or regulatory fees.").

7. *E.g.*, Covell v. City of Seattle, 127 Wash. 2d 874, 905 P.2d 324 (1995).

8. *See infra* Part V.

9. *Covell*, 127 Wash. 2d at 879, 905 P.2d at 327.

10. *See infra* notes 188-96.

In Section II, this Article describes the basic characteristics of taxes as that term historically has been understood in Washington State and delineates the protections put in place for taxpayers. Section III discusses the fundamental characteristics of non-tax fees and the different rules that have evolved to protect those who must pay fees and similar rates and charges. Section IV outlines the *Covell* tests and suggests that while those tests were a significant advance over the Supreme Court of Washington's earlier approach, leftover language about the regulatory nature of fees has prolonged the muddle. Section V reviews each of the post-1995 cases that cited *Covell* and demonstrates that the *Covell* framework worked well in some instances while failing in others because of the lingering attempt to squeeze all governmental charges into just two boxes. Specifically, limiting government charges to either taxes or regulatory fees does not take advantage of everything *Covell* has to offer as an analytical guide.[11] The Appendix summarizes the analysis provided in this Article.

II. TAXES: IMPOSED ANYWHERE AND USED FOR ANYTHING— SO LONG AS THE IMPOSITION IS "FAIR"

A. *Imposed Anywhere and Used for Anything*

In the words of a leading public finance economist, "Taxes, the principal means of financing government expenditures, are compulsory payments that do not necessarily bear any direct relationship to the benefits of government goods and services received."[12] From a legal viewpoint, taxation is viewed as a fundamental, necessary, and sovereign power of government.[13] Our Anglo-American political and legal traditions hold that everyone who receives the general benefits of government should pay his or her fair share of the costs to maintain that government.[14] There is constant debate over what constitutes a fair system of taxation and a fair allocation of the tax burden: taxes based on

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11. *See, e.g.*, *Thurston County Rental Owners Ass'n* 85 Wash. App. at 171, 931 P.2d at 208.

12. DAVID N. HYMAN, PUBLIC FINANCE: A CONTEMPORARY APPLICATION OF THEORY TO POLICY 23 (3d ed. 1990).

13. Lawrence v. State Tax Comm'n of Miss., 286 U.S. 276, 279 (1932) ("[T]he most plenary of sovereign powers, [used] to raise revenue to defray the expenses of government and to distribute its burdens equably among those who enjoy its benefits."); Love v. King County, 181 Wash. 462, 467, 44 P.2d 175-77 (1935).

14. *See* JOHN LOCKE, TWO TREATISES OF GOVERNMENT 380 (Cambridge University Press 1970) ("[T]is fit everyone who enjoys his share of the Protection, should pay out of his Estate his proportion for the maintenance of it.").

wealth,[15] on income and ability to pay,[16] on economic activity,[17] or on perceived benefits.[18] A substantial amount of income redistribution and cost-shifting of public goods and services takes place through the tax system.[19] Indeed, we have a broad assortment of taxes imposed to raise money from a variety of sources and activities: real and personal property taxes,[20] leasehold excise taxes,[21] gross business income taxes,[22] retail sales and use taxes,[23] estate taxes,[24] and many others.[25]

What is worth noting about taxes is that there is no connection between the person who bears the burden of a tax dollar and who determines how to spend tax revenue.[26] "Taxes are defined to be 'burdens or charges imposed by legislative authority on persons or property, to raise money for public purposes, or, more briefly, an imposition for the supply of the public treasury.'"[27] Unless the legislature chooses to earmark taxes (which it

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15. HYMAN, *supra* note 12, at 584 (discussing a comprehensive wealth tax base).

16. *Id.* at 489 (discussing taxation of personal income).

17. *See id.* at 556 (discussing the direct taxation of consumption: the expenditure tax).

18. *See id.* at 2 ("We all benefit from government and expenditures. We rely on governments to provide us with such basic services as national defense, education, highways and mass transit, and social programs to maintain the incomes and welfare of the unemployed, the poor, and the elderly.").

19. *See generally* ROBERT P. STRAUSS, A STUDY OF ALTERNATIVE TAX STRUCTURES FOR THE STATE OF WASHINGTON 5-21 (1987).

20. WASH. REV. CODE §§ 84.04.080, .090 (2002).

21. WASH. REV. CODE § 82.29A (2002).

22. WASH. REV. CODE § 82.04 (2002).

23. WASH. REV. CODE §§ 82.08, 82.12 (2002).

24. WASH. REV. CODE § 83.100 (2002).

25. WASH. STATE DEPT. OF REVENUE, TAX REFERENCE MANUAL (2002) [hereinafter TAX REFERENCE MANUAL] (discussing admissions taxes, household taxes, and taxes for streets and roads). For a discussion of city revenue sources, see REVENUE GUIDE, *supra* note 4. In the past, poll taxes ("head taxes" or "capitation" taxes) played a role in Washington public finance, and net income taxes were approved on several occasions by the Legislature and once by the voters. *See generally* PHIL ROBERTS, A PENNEY FOR THE GOVERNOR, A DOLLAR FOR UNCLE SAM: INCOME TAXATION IN WASHINGTON (2002). Alfred Harsch, *The Washington Tax System–How It Grew*, 39 WASH. L. REV. 944 (1965); Hugh D. Spitzer, *A Washington State Income Tax–Again?*, 16 U. PUGET SOUND L. REV. 515 (1993).

26. Gruen v. Tax Comm'n., 35 Wash. 2d 1, 33-34, 211 P.2d 651-70 (1949), *overruled in part by* State *ex rel.* Wash. State Fin. Comm. v. Martin, 62 Wash. 2d 645, 384 P.2d 833 (1963).

27. State *ex rel.* Nettleton v. Case, 39 Wash. 177, 182, 81 P. 554, 556 (1905) (quoting 27 Am. & Eng. Ency. Law (2d ed.) at 578); Hillis Homes, Inc. v. Snohomish County, 97 Wash. 2d 804, 809, 650 P.2d 193, 195 (1982) *superseded by statute* (*Hillis Homes I*); *see also* San Telmo Assoc. v. City of Seattle, 108 Wash. 2d 20, 24, 735 P.2d 673-75 (1986) (stating Seattle's "shifting the public responsibility of providing [low-income] housing to a limited segment of the population . . . is a tax ....").

sometimes does to make a bitter pill easier to swallow), tax revenue may be used for *any* governmental function that lawmakers reasonably determine is a public purpose. Such governmental functions include: public safety;[28] regulatory activities;[29] public facilities;[30] and even for goods usually sold as commodities,[31] such as water or electricity.[32] For accounting purposes, tax revenue may be placed in *any* fund; either the general fund for any use designated by the legislative authority or in an earmarked fund.[33]

An example of the absence of a nexus between the burdens and the benefits of a tax is Washington's cigarette and tobacco tax revenue. Much of this tax revenue is placed in the general fund.[34] However, the Washington State Legislature earmarked a portion of this revenue for various public projects including: financing of water pollution control facilities;[35] health services for low-income people;[36] drug enforcement and education; and criminal justice and crime prevention.[37] Although there may be an attenuated connection between

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28. *See, e.g.*, WASH. REV. CODE § 81.14B.030 (2002) (imposing 911 excise taxes on the use of switchboard access lines and radio access lines).

29. *See infra* notes 197-204.

30. *See, e.g.*, WASH. REV. CODE § 82.14.400 (2002) (imposing sales and use taxes for zoo, aquarium and wildlife facilities).

31. Arguably, some taxes are so earmarked and so related to the activity generated that they are no longer best thought of as taxes at all. For example, Article II, Section 40 of the Washington State Constitution requires that all motor vehicle fuel taxes be "placed in a special fund to be used exclusively for highway purposes." WASH. CONST. art II, § 40. Because there is a direct connection between fuel consumption and road use, the gas tax might be better thought of as a user fee of the "burden offset charge" variety. *See infra* notes 42-56 and accompanying text.

32. *See* WASH. REV. CODE § 82.32.390 (2002).

33. *See, e.g.*, WASH. REV. CODE § 82.32.380 (2002) (requiring the State Treasurer to deposit excise taxes in "the state general fund or such other fund as may be provided by law"); WASH. REV. CODE § 82.14B.030 (taxing emergency services communications systems).

34. *See* WASH. REV. CODE § 82.32.380.

35. WASH. REV. CODE § 82.24.027 (2002) (depositing monies collected from additional tax "upon the sale, use, consumption, handling, possession, or distribution of cigarettes" into the water quality account); WASH. REV. CODE § 82.26.025 (2002); WASH. REV. CODE § 82.32.390 (2002) (accepting monies received from the imposition on sales or use of articles of tangible personal property which become or are to become part of the new or existing water pollution control facilities and activities); WASH. REV. CODE § 70.146.030 (2002).

36. WASH. REV. CODE § 82.24.020 (2002) (depositing monies collected from additional tax "upon the sale, use, consumption, handling, possession, or distribution of all cigarettes" into the health services account); WASH. REV. CODE § 82.26.020 (2002); WASH. REV. CODE § 43.72.900 (2002) (defining health services account).

37. WASH. REV. CODE § 82.24.020 (depositing monies collected from additional tax "upon the sale, use, consumption, handling, possession, or distribution of all cigarettes" into the health services account); WASH. REV. CODE § 69.50.020 (2002) (designating receipts from WASH. REV. CODE § 82.24.020, among others, to be deposited into the violence and drug

low-income smokers and their use of public health services, there certainly is no link between tobacco users and the beneficiaries of groundwater protection programs.

B. *Taxpayer Protections*

Taxes cast a broad net to raise general revenue for the public purse.[38] Because taxpayers have no guarantee that their dollars will directly benefit them, a number of protections have evolved to assure fairness in the distribution of the tax burden.[39] The burden of the property tax, the oldest major tax in Washington state,[40] must be allocated consistent with the "uniformity provisions" of Article 7, Section 1 of the Washington State Constitution.[41] Without the approval of a supermajority of the voters in a taxing district, the maximum annual tax burden on any piece of property is limited to one percent of its value.[42] Constitutional uniformity requirements do not strictly apply in their entirety to excise taxes.[43] However, those taxes must be uniform within reasonably created legislative classifications.[44] These classifications cannot violate equal protection and may not be arbitrary or abusive.[45] Excise taxes must be geographically uniform.[46]

A further protection for those partially burdened by taxes is the limitation that they may not be imposed except pursuant to express statutory authorization.[47] However, this is only after the prospective taxpayers have an

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enforcement account).

38. *See* REVENUE GUIDE, *supra* note 4 (discussing various taxes designed to raise revenue); HYMAN, *supra* note 12 ("We rely on governments to provide us with such basic services as national defense, education, highways and mass transit, and social programs to maintain the incomes and welfare of the unemployed, the poor, and the elderly.").

39. *E.g.*, WASH. CONST. art. VII, § 1 ("All taxes shall be uniform upon the same class of property within the territorial limits of the authority levying the tax and shall be levied and collected for public purposes only.").

40. Harsch, *supra* note 25, at 945.

41. WASH. CONST. art. VII, § 1; *see* WADE J. NEWHOUSE, CONSTITUTIONAL UNIFORMITY AND EQUALITY IN STATE TAXATION (2nd ed. 1984) (presenting a thorough state-by-state history of American uniformity clauses since colonial times).

42. WASH. CONST. art. VII, § 2.

43. *See* State *ex rel.* Stiner v. Yelle, 174 Wash. 402, 407, 25 P.2d 91, 93 (1933) (citing Brown-Formom Co. v. Kentucky, 217 U.S. 563 (1910)).

44. *Id.*

45. *Id.* at 407-08, 25 P.2d at 93; *see also* Boeing Co. v. State, 74 Wash. 2d 82, 86, 442 P.2d 970, 972 (1968); Texas Co. v. Cohn, 8 Wash. 2d 360, 369, 112 P.2d 522, 527 (1941).

46. Bond v. Burrows, 103 Wash. 2d 153, 157, 690 P.2d 1168, 1170 (1984). A tax levied for state purposes shall be uniform throughout the state; a tax levied for county purposes shall be uniform throughout the county.

47. Hillis Homes v. Snohomish County, 97 Wash. 2d 804, 809, 650 P.2d 193, 195

opportunity to affect the legislative process; the power to tax cannot be inferred.[48] This principle is best illustrated when local governments attempt to impose general revenue-raising measures without explicit authorization.[49]

Taxes, then, are vehicles to raise money for allocation to *any* proper governmental purpose.[50] There is no connection between the property or activities taxed and the use of the proceeds. Further, there is no connection between the burdened taxpayer and the person or group benefitted. Tax money may be deposited in any fund the legislative body elects. In sum, taxes are a broad-brush method of raising revenue.[51] As a result, special protections are built into the taxation process to ensure property taxes are uniform,[52] excise taxes are broadly applied within reasonable classifications,[53] and taxes are never imposed without express statutory authority.[54]

C. *Taxes, Public Goods and "Public Bads"*

Economic theory is helpful in understanding the background of any particular system of taxes and charges.[55] However, one must distinguish between taxes from a *legal* standpoint (*i.e.*, impositions to raise money generally and subject to a particular set of legal protections),[56] and how taxes *function* from an *economic* standpoint (*e.g.*, taxes redistribute income,[57] focus economic resources on certain public goals[58] and projects,[59] and cause businesses and individuals to make certain choices that affect the economy[60]). Additionally, one must be cautious about generalizations concerning economic theory and the application of that theory to law.[61] Taxes are a key source of

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(1982) (*Hillis Homes I*).

48. *Id.* at 808-09, 650 P.2d at 195.

49. *Id.* at 809, 650 P.2d at 195; Carkonen v. Williams, 76 Wash. 2d 617, 627-28, 458 P.2d 280, 286-87 (1969); Cary v. City of Bellingham, 41 Wash. 2d 468, 472, 250 P.2d 114, 117 (1952).

50. *See Hillis Homes I*, 97 Wash. 2d at 809-10, 650 P.2d at 195-96.

51. *See* HYMAN, *supra* note 12, at 23-24.

52. *E.g.*, Wellington River Hollow v. King County, 113 Wash. App. 574, 54 P.3d 213, 220 (2002).

53. *E.g.*, Dean v. Lehman, 143 Wash. 2d 12, 25, 18 P.3d 523, 531 (2001).

54. *Hillis Homes I*, 97 Wash. 2d at 809, 650 P.2d at 195.

55. *See generally* HYMAN, *supra* note 12.

56. *Id.* at 23.

57. *Id.* at 408.

58. *Id.* at 25-26.

59. *Id.*

60. HYMAN, *supra* note 12, at 26.

61. For example, economists correctly observe that taxes are the primary source of funds for "public goods," of which national defense is the classic example: national defense

funds for public services and for government exercise of regulatory powers.[62]

It is also important to note that economists distinguish among pure public goods,[63] congestible public goods,[64] and price-excludable public goods.[65] Some economists identify semipublic goods and mixed (public/private) goods, for which all or a portion of the costs can be allocated through user fees.[66] Economists also recognize the existence of public bads, known as *negative externalities*.[67] For example, public bads are activities that hold a hidden cost to the general public, and for which society does not pay through normal market pricing mechanisms.[68] Professor David Hyman notes, "Air pollution, for example, is a pure public bad if pollutants diffuse in the atmosphere, thereby affecting all individuals, independent of the location of their residence."[69] Unless allocated by government to the responsible parties (internalizing the externalities), such external costs are not mitigated or paid for by those who cause the problem and must be borne by the public at large.[70]

There are a range of public goods and public bads. As governments become more sophisticated and capable of allocating the costs of providing those goods to the users, or recovering the costs of mitigating those bads from their producers, the broad brush of general taxes is no longer the appropriate sole source of revenue to pay for congestible public goods, price-excludable public goods, mixed goods, and public bads.[71] Instead, user charges can be imposed.[72] Over the past century, payment for a number of goods and bads has

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benefits everyone equally and cannot appropriately be charged to any particular group of users. *Id.* at 135.

62. For example, the funding of government public health and inspection programs, zoning, fire safety, building code enforcement and police. *See generally*, TAX REFERENCE MANUAL, *supra* note 25; JOHN J. MIKESELL, FISCAL ADMINISTRATION: ANALYSIS AND APPLICATIONS FOR THE PUBLIC SECTOR (3d ed. 1991).

63. Public goods, like national defense, do not decrease in value as more people "use" them and from which no one can be excluded as a beneficiary. HYMAN, *supra* note 12, at 136.

64. Congestible public goods are goods such as highways, in "which crowding or congestion reduces the benefits to existing consumers when more consumers are accommodated." *Id.* at 156.

65. Price-excludable public goods are goods such as recreational facilities, which can be priced to reduce overall consumption and to help pay for the goods. *Id.* at 156-57.

66. *See, e.g.*, J. Andrew Hoerner, *What's a Tax, Anyway?* (Tax Notes April 24, 1989) *available in* LEXIS, Nexis Library.

67. HYMAN, *supra* note 12, at 97 (emphasis added).

68. *Id.*

69. *Id.* at 137.

70. *See id.* at 105-08.

71. *See id.*

72. Economists sometimes label as a pollution "tax" an imposition on specific polluters that would be treated as a "fee" or "charge" from a legal standpoint. *See, e.g.*, RICHARD A. MUSGRAVE & PEGGY B. MUSGRAVE, PUBLIC FINANCE IN THEORY AND PRACTICE

been shifted from tax revenues to specific users for water, sewer service, garbage handling, and other commodities and services. For example, Seattle did not transfer its sewer operations from a general fund supported agency to a rate-based utility until 1955.[73] Moreover, the city's Solid Waste Collection and Disposal was not transferred from the general fund to a utility until 1961.[74]

From a legal standpoint, these various user charges are distinctly different from taxes—different both in terms of who bears the burdens and benefits and in terms of the distinct legal protections surrounding and regulating the use of those charges.

III. USER FEES: OFFSETTING THE COST OF COMMODITIES, SERVICES, AND BURDENS

There are several different types of user fees and charges recognized in Washington law.[75] They are closely related and generally share certain basic characteristics. First, they are imposed on specific persons, activities, or properties that receive a service or benefit, or that cause negative externalities (public bads) that burden the rest of the population.[76] Second, they come with a distinct set of legal protections to ensure that the level of each charge does not exceed the cost of the service, benefit, or mitigation of the public bad allocated to the person charged and to ensure that the proceeds of the charge are used solely for the provision of services, benefits, or mitigation and *not* used for general governmental purposes.[77]

As shown in the Appendix, by reviewing each type of user fee recognized in Washington, as well as comparing them with each other, we can discern user fees from taxes.

A. *Commodity Charges: Fees Allocated Directly to Consumers of Government Products and Services*

Commodity charges are fees for products or services provided by governments to consumers in a fashion similar to the way private sector businesses provide products or services.[78] Economists often characterize these

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750 (4th ed. 1984).

73. SEATTLE, WASH. ORDINANCE 84390 (1955).

74. SEATTLE, WASH. ORDINANCE 90379 (1961).

75. *E.g.*, WASH. REV. CODE § 35.92.010 (2002) (city water rates); WASH. REV. CODE § 35.87A.010 (2002) (commodity charges).

76. *See, e.g.*, WASH. REV. CODE § 35.87A.010.

77. *See, e.g.*, WASH. REV. CODE § 35.92.010.

78. *See* MIKESELL, *supra* note 62, at 357.

products and services as private goods because they are used by individual consumers rather than the public collectively.[79] Classic examples of governmentally provided commodities are water and electricity.[80] They are often provided by utilities, self-contained government companies focused on the specific product or service.[81] Commodities may also include special services not available to the public at large.[82]

Governmentally imposed commodity charges are often called rates,[83] which have been present in Washington since the 1890s.[84] It was during this time that Washington's government began creating special-purpose utilities, or public enterprises, that provided services, charged rates, and deposited those rates into special funds for use solely to support the enterprises.[85] Early on, those charges were recognized as something different from taxes.[86] In 1909 the Washington Supreme Court rejected the assertion that Spokane's water rates amounted to "an excessive tax on the community," holding "water rates are not taxes."[87] "The consumer pays for a commodity which is furnished for his comfort and use."[88] Fees for special access, or use of a public facility such as a swimming pool, tennis court, toll bridge, ferry or auditorium, can also be appropriately labeled a commodity charge.[89] Such charges can make congestible public goods less congested and ration price-excludable public goods among users while paying for the cost of their use of the facilities.[90] Economists sometimes treat these fees as a way to account, allocate, and pay for *positive* externalities created by these public goods.[91]

Many statutes expressly permit public providers of commodities and services to impose rates and charges.[92] However, under the Accountancy Act,

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79. *Id.*

80. *Id.* at 359.

81. *E.g.*, WASH. REV. CODE § 35.92.010 (granting cities or towns the authority to acquire and maintain their own waterworks).

82. A good example of these is "assessments" within Parking and Business Improvement Areas to pay for street decorations, music, and security. WASH. REV. CODE § 35.87A.010 (2002).

83. *See, e.g.*, WASH. REV. CODE § 35.92.010.

84. 1 WASH. STATE LOCAL GOVERNANCE STUDY COMM'N, A HISTORY OF WASHINGTON'S LOCAL GOVERNMENTS: FINAL REPORT OF THE LOCAL GOVERNANCE COMMISSION 19 (1988).

85. *Id.*

86. *See id.*

87. Twitchell v. City of Spokane, 55 Wash. 86, 89, 104 P. 150, 151 (1909).

88. *Id.*

89. *See* HYMAN, *supra* note 12, at 156-57.

90. *Id.*

91. *See id.* at 160.

92. *See, e.g.*, WASH. REV. CODE § 35.92.010 (2002) (city water rates); WASH. REV.

those rates must be deposited into a special fund,[93] used for the purpose of defraying the expenses of producing the commodity,[94] and then transferred into the general fund.[95] Another protection further ties the imposition of commodity charges to the users of the commodity: rates (including connection charges) typically must be uniform for the same class of customers or service. However, government rate setters have substantial leeway in establishing classes and allocating costs to various groups of customers based on differences in costs of service, operation and maintenance, location of customers, differing types of service, different capital cost allocations, and other matters that present a reasonable difference as a ground for distinction.[96] In contrast to the express statutory authority required for taxes, the power to impose rates and charges for commodities may be inferred from the authority to provide those commodities[97] so long as the charges a customer pays are reasonably proportionate to the customer's allocable share of the capital and operating costs of providing the commodity or service.[98]

B. *Burden Offset Charges: Fees Allocated Directly to Activities that Use Public Resources by Burdening Those Resources*

Burden offset charges are similar to commodity charges. However, instead of being paid by the buyers of *things*, burden offset charges are fees that allocate and recover the cost of ongoing public programs to handle negative impacts from those who cause them.[99] Both commodity charges and burden

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CODE § 35.92.050 (2002) (city electricity charges); WASH. REV. CODE § 36.94.140 (2002) (county water and sewer rates); WASH. REV. CODE § 54.16.040 (2002) (public utility district electricity rates); WASH. REV. CODE § 57.08.005(10) (2002) (water district water rates).

93. WASH. REV. CODE § 43.09.220 (2002).

94. *See id.*

95. WASH. REV. CODE § 43.09.210 (2002).

96. *See, e.g.*, WASH. REV. CODE § 35.92.010; WASH. REV. CODE § 36.94.140; Silver Shores Mobile Home Park, Inc. v. City of Everett, 87 Wash. 2d 618, 623-24, 555 P.2d 993, 996 (1976); Morse v. Wise, 37 Wash. 2d 806, 811-12, 226 P.2d 214, 217 (1951); Lincoln Shiloh Assocs., Ltd. v. Mukilteo Water Dist., 45 Wash. App. 123, 129-30, 724 P.2d 1083, 1086-87 (1986).

97. Hillis Homes, Inc. v. Public Util. Dist. No. 1 of Snohomish County, 105 Wash. 2d 288, 298, 714 P.2d 1163, 1168-69 (1986) (*Hillis Homes II*).

98. *Id.* at 300, 714 P.2d at 1169.

99. There was early recognition of burden offset charges and processing fees as something different from a tax. In the "head money cases," the United States Supreme Court held that a per immigrant tax imposed on ship owners who brought newcomers to America was not a tax at all, but rather a processing fee or mitigation charge. Edye v. Robertson, 112 U.S. 580, 595 (1884). The Court wrote:

> [T]he true answer . . . is that the power exercised in this instance is not the

offset charges are usually called rates. Sewer, garbage, and storm water rates are typical examples of burden offset charges.[100] Economists view these charges as an efficient way of internalizing the costs of negative externalities.[101] The classic example, air pollution caused by a manufacturing plant, produces a cost that, absent government regulation, will be passed on to the general public rather than being internalized in the cost of making the product.[102] The public will breathe the bad air and, over the long term, bear the cost of the pollution. If not controlled or mitigated, the polluter receives an undeserved benefit from the public—the ability to burden others with pollution without having to pay.

One approach to resolve this problem is to regulate polluters by requiring equipment to be placed in the emission causing device.[103] The cost of handling the pollution will then be directly allocated to the manufacturer and internalized in the cost passed on to consumers of the manufactured product rather than to the public at large.[104] In this example, the government exercises its police power and regulates by forcing the manufacturer to take a specific action to offset its burden on society.[105]

Another way government can cause an offset and internalization of the cost of negative externalities is through direct government action.[106] The government directly alleviates the specific problem and charges the producer of the externality to fund the government's action.[107] This is not a regulatory activity. Rather, it is an alternative to regulation; an alternative that approaches the problem through a government service provider that is often organized as a separate utility.[108] Traditional examples are municipal collection and handling

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> taxing power. . . . The title of the act, "An Act to regulate immigration," is well chosen. It describes, as well as any short sentence can describe it, the real purpose and effect of the statute. Its provisions, from beginning to end, relate to the subject of immigration, and they are aptly designed to mitigate the evils inherent in the business of bringing foreigners to this country, as those evils affect both the immigrant and the people among whom he is suddenly brought and left to his own resources.

Id.

100. *See* WASH. REV. CODE § 35.21.120-.158 (2002); WASH. REV. CODE § 35.67.300-.331 (2002). *See generally* Teter v. Clark County, 104 Wash. 2d 227, 704 P.2d 1171 (1985).

101. *See* MUSGRAVE & MUSGRAVE, *supra* note 72, at 743.

102. *See id.* at 744-45.

103. *See id.* at 747.

104. *See id.* at 747-48.

105. *See id.* at 750.

106. *See generally* WASH. REV. CODE §§ 35.21.120-.158 (2002); WASH. REV. CODE §§ 35.67.300-.340 (2002) (permitting cities to create sewage and garbage systems and utilities).

107. *See* WASH. REV. CODE §§ 35.21.120-.158, 35.67.300-.340.

108. *See* WASH. REV. CODE §§ 35.21.120-.158, 35.67.300-.340.

of garbage and wastewater, both of which prevent human activities from causing public health problems.[109] Those who pay garbage and sewer rates are not paying for government provided *commodities* like water or electricity.[110] However, they are, just the same, users of a governmentally provided system established to handle or mitigate the external impacts caused by their own activities. Burden offset charges such as garbage and sewer rates allocate and internalize his or her proportionate share of the total cost of handling negative externalities of human activity—the production of garbage and sewage.[111]

In *Teter v. Clark County*, the Supreme Court of Washington treated storm water systems in the same fashion as garbage and sewage programs, permitting a government to impose on a property owner his allocable share of the cost of a public surface water system established to handle runoff from his and others' land.[112] The court labeled these payments tools of regulation (and not taxes) because of their direct connection to and payment for a system of dealing with the negative public impacts of private activities.[113] Although Clark County could (and did) directly regulate each landowner's use of property in order to minimize surface water runoff, the county system of storm water ditches, pipes, catch basins, and diversion ponds was not so much a *regulatory* activity as it was a *utility*.[114] Consequently, the cost could be allocated by user fees to those who burden the public environment (and burden downstream private property owners) by the way they use their own private property.[115]

Despite the fact that Mr. Teter did not receive a commodity or a direct service, he was a user of the storm water system just as a homeowner uses a sewage system each time he flushes the toilet.[116] In each case, a system is established to allocate, through fees, the external impacts of human activity to those engaged in that activity, and to internalize and offset the cost of handling the public bads arising therefrom.[117] Applying the traditional standards and protections applicable to user charges, the *Teter* court held the storm water charges proper so long as the fees reflected the user's allocable share of the costs of the program, were used solely for the costs of that program, and were

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109. *See, e.g.*, WASH. REV. CODE § 35.21.120-.158, 35.67.300-.340.

110. *See, e.g.*, City of Spokane v. Carlson, 73 Wash. 2d 76, 84, 436 P.2d 454, 459 (1968) (upholding mandatory municipal collection of inorganic garbage when the plaintiff challenged a city that barred him from disposing of that solid waste on his own).

111. *Id.*

112. 104 Wash. 2d 227, 237-38, 704 P.2d 1171, 1179 (1985).

113. *Id.* at 239, 704 P.2d at 1180.

114. *See id.* at 240-41, 704 P.2d at 1181.

115. *Id.* at 237, 704 P.2d at 1179.

116. *Id.* at 232, 704 P.2d at 1176.

117. Teter v. Clark County, 104 Wash. 2d 227, 232-34, 704 P.2d 1171, 1176-78 (1985).

not siphoned off into the general fund.[118] Furthermore, if burden offset fees are disproportionately high, they run the risk of being challenged as an unconstitutional taking.[119]

The Washington State Supreme Court has sometimes stated that if a user fee is higher than the user's proportionate share of program costs, then the fee becomes fiscal in character and is therefore a tax.[120] It is correct that if an imposition is made to raise money for general public purposes, it is a tax.[121] However, the fact that a particular user charge exceeds the user's fair share does not automatically convert that charge into a tax.[122] After all, the excess revenue might continue to be deposited into the appropriate special fund for utility purposes.[123] If a user charge is too high, it is just too high. When the size of the charge exceeds the proportionate share rule and the service classification rule, the excess amount can be rejected on that basis alone. Similarly, if a property tax exceeds legal limits or is not applied uniformly it does not lose its basic character as a tax—it is simply rejected for failure to conform to a protection inherent to taxes.[124]

Growth impact fees under Washington Revised Code sections 82.02.050-.090, transportation fees under Washington Revised Code chapter 39.92, and conditions or charges tied directly to property development are a slightly different form of burden offset charge.[125] Growth impact fees are imposed on developers to pay for public parks and open space, streets and roads, and schools and fire protection facilities.[126] Moreover, they are identified in capital facilities plans and have been demonstrated to serve, or to be "necessitated by"

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118. *Id.* at 233-34, 704 P.2d at 1177.

119. This Article is not meant to provide an analysis of the many cases relating to whether regulatory actions, or exactions, constitute takings. Nevertheless, it should be noted that if governments properly observe the legal protections constraining the level of user charges (*i.e.*, if the imposition of a charge relates to the payor's activities and if the amount of the charge reflects the payor's allocable share of the project or program designed to handle the effect of those activities) a takings challenge to a specific burden offset charge or impact fee will likely fail. *See generally*, Commercial Builders of N. Cal. v. City of Sacramento, 941 F.2d 872, 875 (9th Cir. 1991); Margola Assocs. v. City of Seattle, 121 Wash. 2d 625, 643-48, 854 P.2d 23, 33-36 (1993); Guimont v. Clarke, 121 Wash. 2d 586, 603-08, 854 P.2d 1, 10-13 (1993); Jordan v. Vill. of Menomonee Falls, 137 N.W. 2d 442, 446-47 (Wis. 1965).

120. *See, e.g.*, Margola Assocs. v. City of Seattle, 121 Wash. 2d 625, 640, 854 P.2d 23, 29 (1993).

121. *Id.*

122. *See Teter*, 104 Wash. 2d at 238-39, 704 P.2d at 1080.

123. *See generally* WASH. REV. CODE § 82.02.070 (2002).

124. *See* WASH. CONST. art VII, § 1.

125. *See* WASH. REV. CODE § 82.02.050 (2002).

126. *Id.*

and "reasonably related to," specific developments.[127] Growth impact fees must be deposited in special interest-bearing accounts[128] and, if not used within a limited time period, are refunded to the developer.[129] Transportation impact fees imposed under Washington Revised Code chapter 39.92 also fit in this category.[130] Both types of impact fees are offset payments to compensate for externalities caused by specific developments—by the burden or increased use of public facilities caused by the development.[131]

Similarly, project-specific fees required as a permit condition to pay for direct project impacts are burden offset charges, which must be proportionate and deposited in a special fund for use solely for the related public improvements.[132] Growth impact fees and transportation impact fees are similar to other burden offset charges. The difference is that impact fees are paid just once and may be held for future capital projects rather than being imposed on an ongoing basis for a continuing system or program.[133]

C. *Inspection and Processing Fees (True "Regulatory Fees")*

Inspection fees and processing fees are charges to people who ask the government to pay them special attention, or whose activities give rise to special regulatory oversight.[134] In either case, governments must allocate resources to those projects or activities. Examples are building permit fees,[135] septic or sewer installation charges,[136] the portion of water connection fees used

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127. WASH. REV. CODE §§ 82.02.060(1)(a), .090(3) (2002).

128. WASH. REV. CODE § 82.02.070(1).

129. WASH. REV. CODE § 82.02.080 (2002).

130. WASH. REV. CODE § 39.92.040 (2002).

131. *See* WASH. REV. CODE § 82.02.050.

132. State *ex rel.* Myhre v. City of Spokane, 70 Wash. 2d 207, 216, 422 P.2d 790, 795-96 (1967); Southwick, Inc. v. City of Lacey, 58 Wash. App. 886, 890-93, 795 P.2d 712, 714-16 (1990); Miller v. City of Port Angeles, 38 Wash. App. 904, 909-10, 691 P.2d 229, 234 (1984).

133. Mitigation fees imposed under the State Environmental Policy Act (WASH. REV. CODE § 43.21C.060) are also appropriately classified in the "burden offset fee" category. Required mitigation activities or payments must relate directly to the negative externalities caused by a development and identified in environmental documents; the mitigation must be reasonable; and there must be a nexus between the level of the exaction, the use of the mitigation payments and the development itself. WASH. REV. CODE § 43.21C.060 (2002). *See* RICHARD L. SETTLE, THE WASHINGTON STATE ENVIRONMENTAL POLICY ACT, A LEGAL AND POLICY ANALYSIS § 18(b) at 230-31 (Revised Ed. 2002).

134. *See generally infra* text accompanying notes 135-40.

135. *E.g.*, SEATTLE, WASH. MUN. CODE §§ 3.06.050, 22.504.010, 22.900D.010 (2002).

136. *E.g.*, WASH. REV. CODE § 57.08.005(10) (2002).

for an inspector to check a new hookup,[137] housing registration and inspection fees,[138] professional licensing fees,[139] and driver's license examination fees that are used to process an individual's application and exam.[140] These fees are used to pay for the share of the burden an activity places on government operations;[141] such fees are not permitted to exceed the proportionate share of providing governmental oversight of the regulated activity.[142]

These fees are true regulatory fees in that each one is charged to cover the cost of a regulatory program.[143] These charges often fund a part of the cost of public health, building inspections, and other police power activities that otherwise would be financed by taxes.[144] They provide a pinpointed allocation of costs to specific users or activities, thus relieving costs to the general public.[145] If, and to the extent, inspection and processing fees exceed the allocable share of a government police power activity, they may be held to be unlawful as a type of hidden tax to raise general revenue.[146]

D. *Special Assessments*

Special assessments have occasionally been referred to as special taxes.[147]

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137. *E.g.*, SEATTLE, WASH. MUN. CODE § 21.04.020 (2002).

138. *E.g.*, SEATTLE, WASH. MUN. CODE § 22.900F.040 (2002).

139. *E.g.*, WASH. REV. CODE §§ 18.106.125, 18.140.050 (2002).

140. *E.g.*, WASH. REV. CODE § 46.20.120 (2002).

141. *See supra* text accompanying notes 135-40.

142. *See supra* text accompanying notes 135-40.

143. *See supra* notes 135-40.

144. Even the state is required to pay local government fees for its share of the cost of filing and processing documents. State v. Grays Harbor County, 98 Wash. 2d 606, 607-10, 656 P.2d 1084, 1085-86 (1983).

145. *See supra* notes 135-40.

146. Margola Assocs. v. City of Seattle, 121 Wash. 2d 625, 640, 854 P.2d 23, 31 (1993).

147. *See, e.g.*, State *ex rel.* Frese v. City of Normandy Park, 64 Wash. 2d 411, 422, 392 P.2d 207, 214 (1964); East Hoquiam Co. v. City of Hoquiam, 90 Wash. 210, 215, 219, 155 P.2d 754, 756-57 (1916). However, Article VII, Section 9 of the Washington Constitution, which authorizes special assessments, empowers local governments "to make local improvements by special assessment, or by special taxation of property benefited." This language suggests that special assessments are something different from "special taxation," which might be a tax that is not uniform throughout a taxing district and is thus different from ordinary local government taxes that Article VII, Section 9 requires to be "uniform in respect to persons and property within the jurisdiction of the body levying the same." WASH. CONST. art. VII, § 9; Berglund v. Tacoma, 70 Wash. 2d 475, 477, 423 P.2d 922, 923 (1967) (stating that "[s]pecial assessments . . . are not deemed taxes" for purposes of "uniformity provisions of the state constitution"); *see also* Smith v. City of Seattle, 25 Wash. 300, 315, 65 P. 612, 617 (1901) (holding that special assessment bonds do not count against a municipality's limit on bonds payable from taxes).

Conceptually, however, they are not taxes at all. They are, rather, a distinctive form of user charge which allocates the cost of public improvements that increase the value of an asset (property) to the owner of that asset.[148] Like other user fees, the amount of special assessments must relate directly to the cost of the improvements, relate to the value of the improvements to the property assessed, and be deposited in special accounts for the particular improvements.[149] Among the various types of user charges, assessments are similar to commodity charges because they both allocate costs of *positive* externalities to those who benefit from a service, product, or (in the case of special assessments) an improvement.[150]

IV. *COVELL* HELPS PART OF THE WAY THROUGH THE MUDDLE

Much of law is taxonomic in nature. That is, it involves classifying activities by people and institutions so that rules of human conduct can be developed and readily applied to future conduct. To be effective, classifications have to make sense. Courts sometimes apply labels, that on first blush seem to fit, without sufficiently analyzing the underlying characteristics of the activity concerned.[151] In the case of taxes, fees, rates, and charges, Washington court opinions prior to *Covell v. City of Seattle*[152] failed to distinguish the fundamental characteristics of taxes from those of user charges.[153]

The big culprit was *Hillis Homes, Inc. v. Snohomish County* ("*Hillis Homes I*"), which in 1982 simplistically divided Washington State's revenue world into two parts: taxes and regulatory fees.[154] At issue in that case were county charges imposed on developers to offset the burdens their projects

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148. WASH. CONST. art. VII, § 9.

149. Bellevue Assocs. v. City of Bellevue, 108 Wash. 2d 671, 674-75, 741 P.2d 993, 995-96 (1987); Philip A. Trautman, *Assessments in Washington*, 40 WASH. L. REV. 100, 118 (1965).

150. When improvements paid by assessments also have general public benefits, Washington's Supreme Court has left to the legislative authority the choice of how best to allocate the cost of those benefits between general beneficiaries and special users. *See, e.g.*, City of Seattle v. Rogers Clothing for Men, 114 Wash. 2d 213, 228, 787 P.2d 39, 47 (1990); *In re* Aurora Avenue, 180 Wash. 523, 529-32, 41 P.2d 143, 145-47 (1935).

151. *See* Hillis Homes, Inc. v. Snohomish County, 97 Wash. 2d 804, 809, 650 P.2d 193, 195 (1982) (*Hillis Homes I*).

152. Covell v. City of Seattle, 127 Wash. 2d 874, 905 P.2d 324 (1995).

153. *See* Hillis Homes, Inc. v. Pub. Util. Dist. No. 1 of Snohomish County, 105 Wash. 2d 288, 299, 714 P.2d 1163, 1169 (1986) (*Hillis Homes II*) (citing Teter v. Clark County, 104 Wash. 2d 227, 239, 704 P.2d 1171, 1180 (1985)) (reaffirming that the difference between a fee and a tax is that taxes are to raise revenue while fees are to regulate).

154. *Hillis Homes I*, 97 Wash. 2d at 809, 650 P.2d at 195.

placed on roads, schools, parks, and fire protection.[155] The court labeled the fees as unauthorized taxes: "If the fees are merely tools in the regulation of land subdivision, they are not taxes. If, on the other hand, the primary purpose of the fees is to raise money, the fees are not regulatory, but fiscal, and they are taxes."[156] That statement caused a great deal of subsequent confusion because the taxes versus regulatory fee construct neither adequately describes the full range of governmental charges nor provides useful guidance for judges trying to label such charges in later cases.

Taxes *are* to raise money;[157] yet, so are fees.[158] Municipal water utilities do not charge rates for any purpose other than to raise money.[159] However, that does not transform those rates into taxes; nor are water rates *regulatory tools*, as the Washington Supreme Court labeled water connection charges in *Hillis Homes v. Public Utilities District No. 1 of Snohomish County* ("*Hillis Homes II*").[160] The same problem arose in *Teter v. Clark County,* where the court described storm water charges as *regulatory fees* because the system in question was involved with the "regulation and control of storm and surface waters."[161] The term *regulatory fees* should be restricted to charges on people or property subject to regulation, not to the regulation of water usage or storm water flow. Properly understood, *regulatory fees* are charges to cover the cost of the state's use of its regulatory powers which can be allocated to those who are either voluntarily or involuntarily receiving special attention from government regulators.[162] Such fees cover public expenditures on inspection, record-keeping, and processing, and are correctly limited to the proportionate cost of giving the fee payer that special attention.[163]

Regulatory fees are only one variety, a rather narrow variety, of user fees.[164] So what are water connection charges and storm water utility fees? They are *not* regulatory fees. Instead, they are a different subspecies of user

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155. *Id.* at 806, 650 P.2d at 194.

156. *Id.* at 809, 650 P.2d at 195.

157. *Id.*

158. *See Teter*, 104 Wash. 2d at 234, 704 P.2d at 1177.

159. WASH. REV. CODE § 35.92.010 (2002); Twitchell v. City of Spokane, 55 Wash. 86, 88, 104 P. 150, 151 (1909).

160. 105 Wash. 2d 288, 299, 714 P.2d 1163, 1169 (1986) (*Hillis Homes II*) (approving those charges by squeezing them into the only available non-tax box, the court stated "the District has exacted a connection charge from its new water system customers as part of an overall plan to regulate the use of water").

161. 104 Wash. 2d at 239, 704 P.2d at 1180.

162. Covell v. City of Seattle, 127 Wash. 2d 874, 879-90, 905 P.2d 324, 327 (1995).

163. *See Teter*, 104 Wash. 2d at 239, 704 P.2d at 1180.

164. *See id.* (explaining that the fees can only be used for regulating specific activities for which they are collected, making them narrow in scope).

fees: a commodity charge in the case of water[165] and a burden offset charge in the case of storm water control.[166] The outcome in court may be the same because in neither instance are we dealing with taxes. However, it turns out to be helpful if the taxonomy is correct.

Covell made a real advance in discerning between taxes and the various types of user fees.[167] That case involved street utility charges levied by the City of Seattle on residential properties.[168] Although the court was split as to whether the particular charges in question were taxes or user fees, there was uniform agreement on the factors to consider:[169]

- First, is "'the primary purpose ... to accomplish desired public benefits which cost money, or [is] the primary purpose ... to regulate[?]'"[170]
- Second, is "the money collected allocated ... only to the authorized ... purpose[?]"[171]
- Third, is there "a direct relationship between the fee charged and the service received by those who pay the fee or between the fee charged and the burden produced by the fee payer[?]"[172]

The *Covell* classifications represented a leap in sophistication. *Covell* recognized that there are different types of user fees—some for the cost of direct regulatory activities,[173] some for the cost of commodities purchased,[174] and others for costs (burdens) imposed on the general public by specific human activities.[175] After applying the factors listed above, the majority in *Covell* determined that the street utility charges in question were hidden property taxes.[176] Although the money was allocated for a specific purpose, the charges were (like property taxes) inescapably imposed on all residential property regardless of whether or not someone was in residence and using the streets.[177]

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165. Twitchell v. City of Spokane, 55 Wash. 86, 89, 104 P. 150, 151 (1909).

166. *Teter*, 104 Wash. 2d at 234-36, 704 P.2d at 1178 (determining that the appellants' properties added to the burden of storm water control by increasing the amount of surface water the facilities were forced to handle).

167. 127 Wash. 2d at 879, 905 P.2d at 327.

168. *Id.* at 876, 905 P.2d at 325.

169. *Id.* at 879, 905 P.2d at 327.

170. *Id.*

171. *Id.*

172. *Covell*, 127 Wash. 2d at 879, 905 P.2d at 327.

173. *Id.* at 881, 905 P.2d at 328.

174. *See id.* at 889, 905 P.2d at 332.

175. *Id.* at 888-89, 905 P.2d at 331.

176. *Id.* at 891, 905 P.2d at 333.

177. *Covell*, 127 Wash. 2d at 890, 905 P.2d at 332.

Furthermore, the amount of the charges was not individually determined and the city could not prove a direct relationship between the fee and service or between the fee and burden produced.[178] Consequently, Seattle's version of a residential street utility charge failed the first and third *Covell* tests for distinguishing a user fee from a tax.[179]

Yet, *Covell* failed to move the analysis forward in one important respect: in the first factor it clung to the *Hillis Homes I* conceptual dichotomy between a tax-to-raise-money on the one hand, and a regulatory-fee-to-regulate on the other.[180] It implicitly recognized the variety of user fees and the fact that user fees *are* to raise money for a specific purpose rather than for the general fund.[181] Unfortunately, the court did not make those concepts as explicit as it might have.[182] The *Covell* court failed to observe that the key question is not whether a charge is to raise money, but to raise money *for what*? Is the financial imposition to raise money to pay for public goods? For general government? For any public purpose? If so, it is probably a tax. Is the charge to raise money for a specified government service or program with the charge allocated only to those who receive the service or cause a burden? If so, it is probably a user fee.[183] The *Covell* court appears to have understood this distinction, but did not make it as explicit as it could have. Nor did the court relegate regulatory fees to the narrow subcategory of user charges to which they belong. As a result, later cases have continued to parrot the misleading regulatory fee concept.[184] Nonetheless, Washington appellate decisions since *Covell* have applied the *Covell* factors with a fair degree of consistency, and have on occasion worked around the *Hillis Homes I* analytical trap that lingered on through the first *Covell* factor.

V. THE POST-*COVELL* CASES

In several cases since *Covell*, Washington appellate courts have been

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178. *Id.* at 884-85, 905 P.2d at 329-30. Ironically, motor vehicle fuel tax verges on being appropriately thought of as a burden offset street use charge instead of a tax. Gas taxes paid by drivers relate directly to road use, and by constitutional mandate, gas tax proceeds are deposited in a special fund for road and highway purposes only. *See* WASH. CONST. art. II §40.

179. *Covell*, 127 Wash. 2d at 889, 905 P.2d at 331-32.

180. *Id.* at 879, 905 P.2d at 327.

181. *Id.* at 888-89, 905 P.2d at 331.

182. *See, e.g.*, Thurston County Rental Owners Ass'n v. Thurston County, 85 Wash. App. 171, 179, 931 P.2d 208, 213 (1997) (characterizing a permit program for on-site septic tank systems simply as regulatory fees without further explanation).

183. *Covell*, 127 Wash. 2d at 879, 905 P.2d at 327.

184. *See, e.g.*, *Thurston County Rental Owners Ass'n*, 85 Wash. App. at 180-81, 931 P.2d at 214.

called on to distinguish between taxes and user fees. They have done so with a fair degree of understanding of the underlying distinctions between those two general categories of monetary impositions, and with an apparent recognition of the different subcategories of user fees.

A. Thurston County Rental Owners Ass'n v. Thurston County

The first appellate case to apply the *Covell* factors was *Thurston County Rental Owners v. Thurston County*, a challenge to a county permit system for on-site septic tanks.[185] The relevant ordinance required applicants for new septic system permits to pay a seventy dollar fee, and operators of those systems to pay an annual forty dollar fee.[186] There were between 32,000 and 37,000 septic systems in the county, and the program was structured to gradually bring all units under its purview.[187] Fee revenue was used solely to offset administrative costs and to fund enforcement and inspections.[188] The costs of the program exceeded revenue from the fees.[189] The court of appeals applied the *Covell* tests and held: first, the primary purpose of the fees was regulatory;[190] second, the fee revenue was allocated solely to the authorized purpose; and third, there was a clear relationship between the fee charged and the burden produced by the fee payer.[191]

In many respects this was a true regulatory fee because the money was used to administer a septic system registration and ongoing oversight regulation program. But it also had characteristics of a commodity charge because people who relied on well water were buying additional health protection through the program's efforts. As to septic system owners, the charge was rather like a burden-offset charge because the money was applied in part to address the environmental impacts of their septic systems.[192] However characterized, the program and its fees were upheld in their entirety.[193]

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185. *Id.* at 175-78, 931 P.2d at 211-12.
186. *Id.* at 176, 931 P.2d at 212.
187. *Id.* at 175-76, 931 P.2d at 211.
188. *Id.* at 176, 931 P.2d at 212.
189. *Thurston County Rental Owners Ass'n*, 85 Wash. App. at 176-77, 931 P.2d at 208-12.
190. *Id.* at 179, 931 P.2d at 213.
191. *Id.*
192. *Id.*
193. *Id.* at 175, 931 P.2d at 211.

B. Smith v. Spokane County

The next case to apply the *Covell* framework was *Smith v. Spokane County*,[194] a challenge to aquifer protection area fees imposed on water and sewer customers pursuant to Washington Revised Code chapter 36.36.[195] The fees were fifteen dollars per year on water withdrawal and fifteen dollars per year for on-site sewage disposal.[196] Households served by municipal sewage systems within the area boundaries were exempt from the sewage disposal fee.[197] Proceeds of the charges were spent on water quality monitoring, sewer construction, and program administration.[198] The *Smith* court reviewed the fees in light of each of the three *Covell* factors finding: (1) the charges were not to raise money generally, but to fund a regulatory program; (2) the money was devoted solely to the purpose of protecting and preserving the aquifer and the sole source of water in the area; and (3) all of those paying the fee were receiving the direct benefit of the program.[199]

The opinion was weakly reasoned and contained very little analysis. For example, the court did not seem troubled by the fact that the static nature of the flat fees bore no relation to the amount of water consumed or the degree of burden placed on the aquifer by any particular property use.[200] Instead, the opinion characterized the charges as analogous to those in *Teter*, *Hillis Homes II*, and *Thurston County*, and, without much explanation, approved the program in its entirety.[201]

C. Franks & Son, Inc. v. State

Franks & Son, Inc. v. State,[202] involved a challenge to a "gross weight regulatory fee" that had been imposed on trucks operating within the state.[203] The fees provided the sole source of funding for the Washington Utilities and Transportation Commission's motor carrier regulatory and safety enforcement programs.[204] The court held that fees were primarily used for the Commission's

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194. 89 Wash. App. 340, 1348-49, 948 P.2d 1301, 1306 (1997).

195. WASH. REV. CODE § 36.36.030 (2002); *Smith*, 89 Wash. App. at 345, 948 P.2d at 1305.

196. *Smith*, 89 Wash. App. at 346, 948 P.2d at 1305.

197. *Id.*

198. *Id.* at 347, 948 P.2d at 1305-06.

199. *Id.* at 348-51, 948 P.2d at 1306-07.

200. *Id.* at 346, 948 P.2d at 1305.

201. *Smith*, 89 Wash. App. at 352, 948 P.2d at 1308.

202. 136 Wash. 2d 737, 966 P.2d 1232 (1998).

203. *Id.* at 740, 966 P.2d at 1234.

204. *Id.* at 742, 966 P.2d at 1235.

regulatory programs.[205] The plaintiff's challenge was principally that the fee violated the Commerce Clause of the United States Constitution (Art. I, Sec. 8, cl. 3).[206] Whether a Commerce Clause violation existed, depended in part on whether the fee was regulatory or categorized as a tax.[207] The opinion noted "A tax is defined as a levy made for the purpose of raising revenue for a *general governmental purpose*; a fee is enacted principally as an integral part of the regulation of an activity and to cover the cost of regulation."[208] Although the opinion repeated the tax versus regulatory fee construct, it moved a step forward by recognizing that both taxes and user fees raise money, and by expressly noting that a tax is for *general* governmental purposes.[209] Applying the *Covell* factors, the court held that since the charges in question were solely for trucking regulatory and safety programs and appeared not to exceed the allocable costs of those programs, the charges were fees rather than taxes.[210]

D. Harbor Village Apartments v. City of Mukilteo

Harbor Village Apartments v. City of Mukilteo,[211] involved a "residential dwelling unit fee" of $80.60 charged to every rental unit regardless of whether it was actually rented, the number of rental transactions, or income from the unit.[212] The court concluded the fee was a fund-raising mechanism imposed on property that could not be avoided, therefore constituted a property tax.[213] However, Mukilteo's charge was not a permissible excise tax.[214] The flat character of the city's residential dwelling unit fee meant that it bore no relationship to the nature or size of a business transaction and was, therefore, a property tax in disguise.[215] It is interesting to speculate whether the result in the earlier case of *Smith* would have been the same if it had been decided after *Harbor Village Apartments*, since Spokane County's aquifer protection charge was a flat fee, like Mukilteo's rental unit charge.[216] However, there was more

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205. *See id.* at 751, 966 P.2d at 1239.
206. *Id.* at 743, 966 P.2d at 1235.
207. *See Franks & Son v. State*, 136 Wash. 2d at 746, 966 P.2d at 1237.
208. *Id.* at 737, 750, 966 P.2d 1232, 1237 (emphasis added).
209. *See id.* at 749-50, 966 P.2d at 1238-39.
210. *Id.* at 750-51, 966 P.2d at 1239.
211. 139 Wash. 2d 604, 989 P.2d 542 (1999).
212. *Id.* at 604-05, 607, 989 P.2d at 544-45.
213. *See id.* at 607, 989 P.2d at 544-45.
214. *Id.* at 607, 989 P.2d at 545.
215. *Id.* at 607, 989 P.2d at 545.
216. *Compare Harbor Vill. Apartments*, 139 Wash. 2d at 605-06, 989 P.2d at 544, *with* Smith v. Spokane County, 89 Wash. App. 340, 346, 351, 948 P.2d 1301, 1305, 1308 (1997).

direct benefit or burden offset in the Spokane County program.[217] In any event, that program's fees would be unassailable if they had been structured to reflect differences in water usage or sewage output.[218]

E. New Castle Investments v. City of LaCenter

The next case to cite *Covell* was *New Castle Investments v. City of LaCenter*,[219] which addressed the tax versus fee issue in a quite different context: whether "transportation impact fees"[220] vested at the time of preliminary plat approval.[221] Under the vested rights doctrine, permit fees and similar charges related to the grant of a land use permit, vest at the time a land use application is filed.[222] The doctrine does not apply to fees.[223] Here, the court of appeals tried to apply the *Covell* factors to determine whether or not the city's transportation impact fee was a tax or a fee, and thus decide whether or not vested rights existed.[224] In this instance, the attempt to use those factors was something of a failure. The court found the fees resembled taxes because they paid for public facilities (*i.e.*, public goods traditionally paid for by taxes), and because they were set in a broad brush fashion rather than being calculated based on the cost of each new development.[225] The court then changed direction, declining to hold the fees were in fact taxes.[226] Instead, it ruled they were not the *type* of regulatory fees associated with land use control ordinances and protected by the vesting doctrine.[227] In this case, if *Covell* was useful to the court in its analysis, it was not readily apparent in the opinion. The court might have had an easier time if it had recognized that taxes and regulatory fees do not constitute the full array of options, and had considered the possibility that transportation impact fees may simply be a form of burden offset charges.

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217. *See Smith*, 89 Wash. 2d at 350-51, 948 P.2d at 1307.

218. *See generally id.* at 346, 350-51, 989 P.2d at 1305, 1307 (explaining households which do not burden the resources, or burden the resources less would be charged according to use, diminishing complaints of the flat tax charged to all households in the area, absent proof of use).

219. 98 Wash. App. 224, 989 P.2d 569 (1999).

220. WASH. REV. CODE § 82.02.090 (2002).

221. *New Castle Invs.*, 98 Wash. App. at 227-28, 989 P.2d at 571.

222. *See id.* at 231-32, 989 P.2d at 573.

223. *Id.* at 232, 989 P.2d at 573.

224. *Id.* at 233-35, 989 P.2d at 575.

225. *Id.* at 234-35, 989 P.2d at 574.

226. *New Castle Invs.*, 98 Wash. App. at 236, 989 P.2d at 575.

227. *Id.* at 235-36, 989 P.2d at 575.

F. City of Lakewood v. Pierce County

City of Lakewood v. Pierce County,[228] is another muddled case which, like *New Castle Investments*, is constrained by pre-*Covell* thinking that places every governmental charge into one of two boxes.[229] This case arose from the City of Lakewood and Pierce County's inability to agree on a franchise fee amount that the county would pay the city for use of city streets for county sewer lines.[230] The city then attempted to impose the franchise fee on the county.[231] The county responded, in one of its arguments, that under long standing Washington law, a city may not impose a tax without express statutory authorization.[232] The court engaged in a *Covell* factor analysis, concluding the franchise charge was a fee rather than a tax.[233] The court gave three reasons: first, the fee was regulatory in nature; second, the funds would be directed solely to the city's costs of overseeing the county sewer utility's use of the streets; and third, the fee related solely to the burden placed on the city associated with the county's operation of the sewer system under those streets.[234] If franchises are viewed as a mechanism for regulating the use of public right of way, it may be appropriate to characterize franchise fees as true regulatory fees. Alternatively, if franchise fees are rental charges for the use of public facilities, they can be properly treated as commodity charges. In either instance, under rules protecting fee payers, the amount cannot exceed the allocable costs.[235]

But query whether the court needed to have analyzed the situation under *Covell*? The court of appeals in this case ultimately determined that a franchise agreement was a contract and the judiciary was not in the position to force the county to contract with the city or to sign any particular form of agreement or to agree to a specific fee level.[236] Perhaps the tax versus regulatory fee question was inapposite and the entire matter could have been resolved on the grounds that the matter involved neither a tax nor a fee. Indeed, this was just a problem of two municipal corporations unwilling or unable to negotiate a contract—and it would be inappropriate for a court to force them to agree on anything.

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228. 106 Wash. App. 63, 23 P.3d 1 (2001).

229. *See id.* at 74-75, 23 P.3d at 7.

230. *Id.* at 66, 23 P.3d at 3.

231. *See id.* at 66-67, 23 P.3d at 3.

232. *Id.* at 75, 23 P.3d at 7 (citing Carkonen v. Williams, 76 Wash. 2d 617, 458 P.2d 280 (1969)); King County v. Algona, 101 Wash. 2d 789, 681 P.2d 1281 (1984) (involving a similar attempt by a city to impose a tax on a county).

233. *City of Lakewood*, 106 Wash. App. at 75-76, 23 P.3d at 7-8.

234. *Id.*

235. *See id.* at 75-77, 23 P.3d at 7-8.

236. *See id.* at 74, 77-79, 23 P.3d at 7-9.

G. Dean v. Lehman

Dean v. Lehman,[237] is an example of the *Covell* test being usefully applied.[238] Suzanne Dean was the wife of a prison inmate who challenged an automatic statutory deduction of 35% of funds received by inmates, including amounts from spouses.[239] She asserted, among other things, that the deduction was an unauthorized tax; 10% went to an inmate savings account, 20% contributed to incarceration costs, and 5% was transferred to a victim compensation fund.[240] Although many other issues were involved,[241] the supreme court's *Covell* analysis in *Dean* was correct. Under the first *Covell* factor, the court found the purpose of the deduction was not to raise revenue for general governmental purposes, but to pay for specific programs that either benefited the inmates or their victims.[242] Applying the second *Covell* factor, the court noted the funds collected were deposited in special accounts and allocated solely to the programs associated with those accounts.[243] Third, the court found there was a direct relationship between the amounts deducted and either the services received by the inmate, or the amelioration of burdens placed on the community by that inmate.[244] Accordingly, the charges were not taxes.[245] This is another instance where the fees could be analytically viewed as both commodity charges for the prison rent deduction, and burden offset charges for the victim compensation deduction. Although the opinion did not go into that kind of conceptual detail, it clearly knew a non-tax when it saw one, and *Covell* helped that determination to be made.

H. Samis Land Co. v. City of Soap Lake

Samis Land Co. v. City of Soap Lake,[246] was a *Covell* case examining whether a specific governmental charge should be characterized as tax or a fee.[247] In that instance, the city had imposed a flat rate "standby charge" on vacant, unimproved, and uninhabited lots that abutted municipal water and

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237. 143 Wash. 2d 12, 18 P.3d 523 (2001).
238. *See id.* at 26-28, 18 P.3d at 531-32.
239. *Id.* at 15-16, 18 P.3d at 526.
240. *Id.* at 16, 18 P.3d at 526.
241. *See id.* at 18, 18 P.3d at 527.
242. *Dean*, 143 Wash. 2d at 26-27, 18 P.3d at 531-32.
243. *Id.* at 27-28, 18 P.3d at 532.
244. *Id.* at 28, 31, 18 P.3d at 532, 534.
245. *Id.* at 28, 18 P.3d at 532.
246. 143 Wash. 2d 798, 23 P.3d 477 (2001).
247. *See id.* at 801, 23 P.3d at 480.

sewer lines.[248] A property owner challenged the charge on the grounds that it was an unconstitutional, non-uniform property tax.[249] The city argued the charge was associated with a public health program to prevent the spread of communicable diseases through the water supply, the money was deposited into a restricted fund, and the money was used either to provide services or to offset burdens caused by the payers.[250] Therefore, the city argued, the charges were regulatory fees rather than taxes.[251] The state supreme court disagreed, holding that the charges were primarily to finance broad-based public improvements rather than to regulate, and the city's accounting did not sufficiently demonstrate that the money was in fact deposited into a special fund.[252] Most importantly, the opinion noted the uninhabited vacant lots were not receiving any water service, nor did the facts show they were burdening the public with wastewater.[253] Without a direct relationship between the payer and either the service received or burden produced, the charge could not appropriately be considered a user fee.[254]

Soap Lake should be viewed as tracking *Covell* fairly closely. In both cases, the court was troubled by user fees or burden offset charges imposed on properties when the cities had not adequately demonstrated either some directly related benefit or burden.[255] It may be possible for a city to determine that uninhabited houses contribute to street use, or that vacant lots generate waste that needs handling (*e.g.*, vacant/recreational lots on which people camp, thus causing potentially dangerous gray water and human waste). However, neither the City of Seattle in *Covell*,[256] nor the City of Soap Lake in *Soap Lake*,[257] developed facts upon which their respective fees could be sustained. As a result, successful street utility fees and standby charges will have to await a different set of facts and another day.

I. Arborwood Idaho, LLC v. City of Kennewick

Arborwood Idaho, LLC v. City of Kennewick,[258] was a court of appeals

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248. *Id.*
249. *Id.* at 802, 814-15, 23 P.3d at 480, 487.
250. *Id.* at 804-05, 808-10, 23 P.3d at 481-82, 484-85.
251. *Samis Land Co.*, 143 Wash. 2d at 804-05, 23 P.3d at 481-82.
252. *Id.* at 807-11, 23 P.3d at 483-85.
253. *Id.* at 813, 23 P.3d at 486.
254. *Id.* at 811-14, 23 P.3d at 485-87.
255. *See id.* at 811, 813-14, 23 P.3d at 485-87; *see also* Covell v. City of Seattle, 127 Wash. 2d 874, 879, 883-85, 888-89, 905 P.2d 324, 327, 329-31 (1995).
256. *See Covell*, 127 Wash. 2d at 879, 905 P.2d 327.
257. *See Samis Land Co.*, 143 Wash. 2d at 798, 23 P.3d at 477.
258. 113 Wash. App. 875, 55 P.3d 1170 (2002).

evaluation of whether a city's monthly charge for emergency medical services (an ambulance charge) constituted a property tax, an excise tax, or a user charge.[259] The City of Kennewick had imposed the monthly ambulance charge on each occupied residence and business.[260] For residences, the charge was on a per-unit basis and was collected in conjunction with the city's utility bill.[261] If an apartment building (like Arborwood) did not meter utility services to each occupied unit, the city collected the per-unit ambulance charge from the apartment owner and left it to the owner to allocate the charge to each apartment.[262] The *Arborwood* apartment owner contended that if the charge was an excise tax, it was improper because an excise tax must be based on the voluntary action of the person taxed for performing an act and that the apartment owner was not voluntarily subjecting itself by undertaking a specific action.[263] The court in *Arborwood* ruled that although the city could have imposed an excise tax for ambulance services under applicable law,[264] Kennewick had, in this instance, instead imposed a regulatory fee under its general police power.[265] The court of appeals further held that the charge was not a property tax and expressly distinguished the relevant facts from those involved in *Soap Lake* based on the *Covell* factors.[266] The *Arborwood* court held that the ambulance charge was not to raise money for broad-based public improvements, "but instead regulates the fee payers by providing them with a targeted service, a 24-hour emergency service."[267] The court continued that the "targeted service ... alleviates the burden placed on the system by apartment residents."[268] The opinion noted that the second *Covell* factor was satisfied because all money collected from the charge was segregated and used exclusively for the ambulance services, and that the third *Covell* factor was satisfied because there was a direct relationship between the fee charged and the benefit to or burden produced by the fee payer.[269]

Arborwood demonstrates the court's increasing sophistication in applying the *Covell* tests; the *Arborwood* facts were correctly distinguished from those in *Soap Lake*. One of the court's key observations was that in contrast with

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259. *Id.* at 877-78, 55 P.3d at 1171-72.

260. *Id.* at 877-78, 55 P.3d at 1171.

261. *Id.* at 878-79, 55 P.3d at 1172.

262. *Id.* at 880, 55 P.3d at 1172.

263. *Arborwood*, 113 Wash. App. at 883, 55 P.3d at 1174 (citing High Tide Seafoods v. State, 106 Wn.2d 695, 699, 725 P.2d 411 (1986)).

264. WASH. REV. CODE § 35.21.768.

265. *Arborwood*, 113 Wash. App. at 883-85, 55 P.3d at 1174-75.

266. *Id.* at 887, 55 P.3d at 1176.

267. *Id.*

268. *Id.*

269. *Id.* at 888-89, 55 P.3d at 1176-77.

the street utility charge in *Covell* and the standby sewer charge in *Soap Lake*, the Kennewick ambulance charge was not imposed on vacant units.[270] However, the court of appeals need not have referred to the ambulance charge as a "regulatory fee" imposed under the city's general police powers.[271] The opinion correctly conceptualized the emergency medical services system as a utility, and it could have simply treated the fees as utility service charges, which, under *Hillis II*,[272] do not need express statutory authorization. Therefore, the court did not have to use the confusing term regulatory fees to describe Kennewick's ambulance charges. Furthermore, even if Kennewick's ambulance charges were treated as excise taxes, the fact that they were collected by the apartment owner rather than the ultimate users of the service should not have made any difference in the outcome of the case. Washington's tax system already relies on businesses to collect excise taxes from consumers; for example, retail sales taxes are required to be collected by businesses and remitted to the Department of Revenue.[273] In any event, *Arborwood* represents a thoughtful application of the *Covell* tests.

VI. CONCLUSION

Covell moved the tax versus fee analysis by recognizing in its second and third factors that there are different kinds of fees—those for commodities or services purchased, and those for offsetting burdens created by human activity.[274] However, *Covell* retains, in its first factor, a broad use of the term regulatory fee and a repetition of the old mantra that taxes are to raise money while fees are to regulate.[275] This is an example of "epithetical jurisprudence," where a court glues a label on an activity without properly analyzing the underlying concepts behind various available labels to make sure it is applying the right one. It is now time for the Washington Supreme Court to unglue the broad use of the term "regulatory fee" and to limit that concept only to fees paid for processing permits and inspections. By doing so, the court will make explicit an understanding of the underlying concepts that *Covell* implicitly recognized. This will enable judges, lawyers, and the general public to better understand the real nature of charges paid to fund governmental programs.

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270. *Arborwood*, 113 Wash. App. at 889, 55 P.3d at 1177.
271. *See id.*
272. *See supra* note 97 and accompanying text.
273. WASH. REV. CODE § 82.08.050.
274. *See Covell*, 127 Wash. 2d at 879, 881-83 at 327-29.
275. *See id.* at 879, 905 P.2d at 327.

APPENDIX

GENERAL CLASSIFICATION OF TAXES, FEES, AND USER CHARGES

CLASSIFICATIONS	EXAMPLES	BASIC CHARACTERISTICS
TAXES	Property Taxes, Excise Taxes, Income Taxes, certain license fees	Imposed to raise money for *any* governmental purpose. No relationship between tax burden and benefit to an individual taxpayer.
USER CHARGES: Commodity Charges	Electrical rates, water rates, connection charges, irrigation assessments	Imposed to pay for the provision of commodities or services of direct benefit to consumer.
Burden Offset Charges	Sewer rates, garbage rates, storm water utility charges, growth impact fees	Imposed to offset cost of handling burdens on others and on public resources ("externalities") caused by payer's activities.
Processing and Inspection Fees (True "Regulatory Fees")	Building permit fees, housing inspection fees, professional licensing fees, certain other license fees	Imposed to pay costs of governmental handling of payer's applications or requests, or to pay for inspection and control of payer's activities.
Special Assessments	LID, ULID, LUD, RID Assessments	Imposed on property to offset costs of capital improvements that directly increase the value of that property.

GENERAL CLASSIFICATIONS, *Cont'd*

CLASSIFICATIONS	PROTECTIONS	ACCOUNTING
TAXES	Express statutory authority always required. Subject to limits, uniformity requirements and other controls on tax levels and allocation of burden among taxpayers.	May be deposited in general fund or any other funds. May be used for any lawful governmental purpose.
USER CHARGES: Commodity Charges	Commodity charges must be uniform within classes of customers and classes of service. May not exceed allocable share of cost.	Must be deposited in special fund. May not be transferred to general fund or other special funds for purposes of those funds.
Burden Offset Charges	May not exceed payer's allocable share of cost of programs or improvements to handle burdens caused by payer's activities. Must be uniform within classes of service and classes of users. Certain impact fees must be used within certain time periods for identified facilities.	Must be deposited in special fund. May not be transferred to general fund or other special funds. Must be used to pay for program facilities or activities.
Processing and Inspection Fees (True "Regulatory Fees")	May not exceed allocable share of cost of processing, licensing or inspection and enforcement program.	Must be used to pay for processing or program activities.
Special Assessments	May not exceed increase of value of property ("benefit") from improvement. Must be fairly allocated among all benefitted properties.	Must be deposited in special assessment fund or bond fund. May not be transferred to general fund or any other special funds. Must be used for specified improvement.

Appendix C ON-BILL PROGRAM LEGISLATIVE LANGUAGE EXAMPLES

On-Bill Financing/On-Bill Repayment Legislative Bills

State	Program(s)	Bill	Utilities	Loan loss reserve by a municipal utility?*	Loan repayments on the customer's utility bill?	Disconnection for non-payment?	Loan to follow to the meter instead of the person?
Connecticut	Residential, "clean energy" on-bill financing program	House Bill 6350 Public Act No. 13-928 (2011)	Investor-Owned Utilities and Publicly-Owned Utilities	No	Yes	Yes	Yes
Hawaii	Hawaii On-Bill Financing Program (tariff)	Senate Bill 1087(2013)	IOUs and Electric Cooperatives	No	Yes	No	No
Illinois	Illinois Energy Efficiency Loan Program	Senate Bill 2350 (2013)	Utilities providing services to over 100,000 customers	No	Yes	Yes	No
Michigan	Energy Conservation Program	Senate Bill 438 (2016)	All utiltiies	No	Yes	Yes	Yes
New York	On-Bill Loan Recovery Program	Green Jobs—Green New York Act (2009); Power NY Act (2011)	All utiltiies	No	Yes	Yes	Yes
Oregon	Several programs, including Clean Energy Works Oregon (loan); MPower Oregon (loan)	Energy Efficiency and Sustainable Technology Act (2009)	All utiltiies	No	Yes	Yes	Yes
South Carolina	"Help My House" Rural Energy Savings Pilot Program (loan)	Senate Bill 1096 (2010)	All utiltiies	No	Yes	Yes	Yes

Overview of State OBR Legislation

Referencing the legal review provided as Appendix B, the Interior Gas Utility (IGU) is contemplating certain on-bill repayment (OBR) program attributes for which IGU may pursue explicit authorization, they include:

1. IGU sponsored loan loss reserve as mitigation against borrower default.
2. IGU facilitated third party loan collection and repayment through charges on a customer's utility bill.
3. Suspension or termination of service for lack of payment.
4. Loan structured to "follow the meter" and not the customer.

EESI was tasked with identifying model legislative language from which IGU could draft a legislative proposal to solidify its legal authority to operate an OBR program with these attributes.

EESI reviewed enacted on-bill legislation from 13 states. While no single piece of legislation fit all of IGU needs, EESI determined that the best fits were bills from Connecticut, Hawaii, Illinois, Michigan, New York, Oregon, and South Carolina. (The others were California, Georgia, Kentucky, Maine, Massachusetts, and Minnesota.) All seven best-fit states passed language that authorized loan payments charges on the utility bill (Question #2) and all but one included language for disconnection for non-payment (Question #3). Though not expressly determined as a need by IGU counsel, EESI identified language from five states that allows the loan to "follow the meter" (Question #4). None of the bills had explicit language regarding loan loss reserves (Question #1), but some on-bill programs do use loan loss reserves. These are perhaps authorized by separate legislation, which would require additional research to identify.

Please see the attached addendum for a table summary and legislative excerpts from the seven best-fit states that are most relevant to IGU's legislative needs. At IGU's request, EESI can select the best from these excerpts to form model legislative language.

Appendix C: Key Excerpts from State OBR Legislation

Connecticut

Since 2000, United Illuminating (UI), an investor-owned utility, has been running the Small Business Energy Advantage (SBEA) program, an on-bill financing program with internal utility capital for commercial and industrial customers. UI uses utility payment history as underwriting criteria, and disconnection is not allowed for non-payment. Connecticut Light and Power – the other IOU in Connecticut – has been running its own on-bill financing program since 2008.

Starting in June 2011, Connecticut's Home Energy Solutions Program – born out of the 2011 Residential Energy Efficiency Loan Bill – has been offering on-bill repayment loans for residual customers through the two investor-owned utilities. The program is offered to homeowners in single or two-family homes making qualifying energy efficiency improvements. Participants must select an approved contractor for a home energy assessment. Loans range from $2,000 to $20,000 with terms extending out to 10 years.

Connecticut Substitute House Bill 5005 (1998)

Sec. 106. Subsections (e) and (f) of section 32-317 of the general statutes, as amended by section 3 of public act 97-173, are repealed and the following is substituted in lieu thereof:

(e) The commissioner shall adopt regulations in accordance with chapter 54, (1) concerning qualifications for such loans or deferred loans, requirements and limitations as to adjustments of terms and conditions of repayment and any additional requirements deemed necessary to carry out the provisions of this section and to assure that those tax-exempt bonds and notes used to fund such loans qualify for exemption from federal income taxation, (2) providing for the maximum feasible availability of such loans or deferred loans for dwelling units owned or occupied by persons of low and moderate income, (3)establishing procedures to inform such persons of the availability of such loans or deferred loans and to encourage and assist them to apply for such loans and (4) providing that (A) the interest payments received from the recipients of loans or deferred loans, less the expenses incurred by the commissioner in the implementation of the program of loans, deferred loans and loan guarantees under this section, and (B) the payments received from electric, ELECTRIC DISTRIBUTION and gas companies under subsection (f) of this section shall be applied to reimburse the General Fund for interest on the outstanding bonds and notes used to fund such loans or deferred loans.

(f) Not later than August first, annually, the commissioner shall calculate the difference between (1) the weighted average of the percentage rates of interest payable on all subsidized loans or deferred loans made from the energy conservation loan program authorized under sections 32-315 to 32-318, inclusive, AS AMENDED BY THIS ACT, and (2) the average of the percentage rates of interest on any bonds and notes issued

pursuant to section 3-20, which have been dedicated to the energy conservation loan program under sections 32-315 to 32-318, inclusive, AS
AMENDED BY THIS ACT, and used to fund such loans or deferred loans, and multiply such difference by the outstanding amount of all such loans or deferred loans, or such lesser amount as may be required under Section 103 (b)(2) of the Internal Revenue Code of 1986, or any subsequent corresponding internal revenue code of the United States, as from time to time amended. The product of such difference and such applicable amount shall not exceed six per cent of the sum of the outstanding principal amount at the end of each fiscal year of all loans or deferred loans made under the energy conservation loan program authorized under sections 32-315 to 32-318, inclusive, AS AMENDED BY THIS ACT, and the balance remaining in the energy conservation revolving loan account. Not later than September first, annually, the Department of Public Utility Control shall allocate such product among each electric, ELECTRIC DISTRIBUTION and gas company having at
Least seventy-five thousand customers, in accordance with a formula taking into account, without limitation, the average number of residential customers of each company. Not later than October first, annually, each such company shall pay its assessed amount to the commissioner.
The commissioner shall pay to the State Treasurer for deposit in the General Fund all such payments from electric, ELECTRIC DISTRIBUTION and gas companies, and shall adopt procedures to assure that such payments are not used for purposes other than those specifically provided in this section.
The department shall include each company's payment as an operating expense of the company for the purposes of rate-making under section 16-19,
AS AMENDED BY THIS ACT.

Substitute House Bill (HB) 6360 (2013)

Establishes a comprehensive residential clean energy on-bill repayment program financed by third-party private capital managed by the Clean Energy Finance and Investment Authority.

Disconnection for non-payment:

Section (Sec.) 58(b)(8). To authorize the disconnection for nonpayment by the customer of any financing repayment amount, with any on-bill repayment amount treated as part of the customer's utility account subject to the protections provided in Sec. 16-262c, 16-262d, 16-262g to 16-262i, inclusive, and Sec. 16-262x of the general statutes;

Loan repayment on the bill:

Sec. 58(b)(11). To provide that the on-bill repayment billing and collection services shall be available without regard to whether the energy or fuel delivered by the utility is the customer's primary energy source.

Follows the meter:

Sec. 58(b)(10). To provide the assignment of repayment obligations to subsequent owners of the dwelling unit upon the development by the Energy Conservation Management Board and the Clean Energy Finance and Investment Authority of timely written notice guidelines to subsequent owners, except on-bill repayment amounts may not be directly charged to a tenant of a dwelling unit by a utility company pursuant to Sec. 16-262e of the general statutes or a receiver pursuant to Sec. 16-262f, 16-262t, 47a-14h and 47a-56a to 47a-56k, inclusive, of the general statutes.

Hawaii

On-Bill Repayment program in design stage.

S 1087 (2013)

Establishes the Hawaii Green Infrastructure Authority (HGIA) within the Department of Business, Economic Development and Tourism (DCEDT) to acquire and provide alternative low-cost financing, to be deployed through a financing program to make green infrastructure installations (e.g., energy efficiency and clean energy).

Loan repayment on the bill:

Sec. 269-C (c)(7). A requirement that the electric utilities, including any successors, serve as agents to collect the green infrastructure fee and transfer those surcharges to the trustee or other financing party as required by the financing order and any agreements with the department;

Sec. 269-L Electric utilities; cost recovery; billing agent.

(a) The public utilities commission shall ensure that all reasonable costs incurred by electric utilities to start up and implement the loan program may be recovered as part of the electric utility's revenue requirement, including necessary billing system adjustments, costs arising out of the billing and collection of green infrastructure charges, and any costs for green infrastructure charges that are not recovered via participating customers' green infrastructure bill payments, or otherwise…

(c) The loan program or the act of serving as an agent to bill and to collect the green infrastructure charge shall not cause any electric utility to be subject to the laws that regulate financial institutions, escrow depositories, or collection agencies. An electric utility shall not be responsible for lending, underwriting, and credit determinations.

Disconnection for non-payment:

Sec. 269-K(a). The public utilities commission may issue a program order authorizing the allocation … of any amounts deposited or held in the green infrastructure special fund …

Sec. 269-K (c). The order shall specify the following, including: (1) The procedures to be followed by the electric utilities in the event of non-payment or partial payment of the green infrastructure fee by the electric utilities' customers, which procedures shall be

consistent with the public utilities commission approved procedures for non-payment and partial payment of rates, charges, and fees under the electric utilities' tariffs;…

Illinois

The Illinois Energy Efficiency Loan (IEEL) program, launched in 2011, is operated on behalf of the five participating utilities (all IOUs) – Ameren, Commonwealth ComEd, Nicor Gas, North Shore Gas, and Peoples Gas – by RenewFinancial.

SB 1918 (2009)

Loan repayment on the bill: YES

Sec. 19-140. On-bill financing program; gas utilities.

> (a) The Illinois General Assembly finds that Illinois home and businesses have the potential to save energy through conservation and cost-effective energy efficiency measures. Programs created pursuant to this Section will allow utility customers to purchase cost-effective energy efficiency measures with no required initial upfront payment, and to pay the cost of those products and services over time on their utility bill.
>
> (b) Notwithstanding any other provision of this Act, a gas utility serving more than 100,000 customers on January 1, 2009, shall offer a Commission-approved on-bill financing program ("program") that allows its retail customers who own a residential single family home, duplex, or other residential building with four or less units, or condominium at which the gas service is being provided (i) to borrow funds from a third party lender in order to purchase gas energy efficiency measures approved under the program for installation in such home or condominium without any required upfront payment and (ii) to pay back such funds over time through the gas utility's bill...

Sec. 19-140 (c)(6). The gas utility shall remit payment in full to the lender each month on behalf of the participant. In the event a participant defaults on payment of its gas utility bill, the gas utility shall continue to remit all payments due under the program to the lender, and the utility shall be entitled to recover all costs related to a participant's nonpayment through the automatic adjustment clause tariff …

Follows the meter: No

Sec. 19-140 (c)(5). A loan issued to a participant pursuant to the program shall be the sole responsibility of the participant, and any dispute that may arise concerning the loan's terms, conditions, or charges shall be resolved between the participant and lender. Upon transfer of the property title for the premises at which the participant receives gas service from the utility or the participant's request to terminate service at such premises, the participant shall pay in full its gas utility bill, including all amounts due under the program, provided that this obligation may be modified as provided in Subsection (g) of this Section. Amounts due under the program shall be deemed amounts owed for residential and, as appropriate, small commercial gas service.

Proposed amendment by SB 2350 (2013) [amendment failed]:

(4.3). The obligation created by a loan issued under the program shall run with the meter. For the purposes of this Section, "run with the meter" means all of the following:

(A) any portion of a loan issued under the program that remains outstanding prior to sale or transfer of the applicable real property, survives a change in ownership, tenancy, or meter account responsibility;

(B) any portion of a loan issued under the program that remains outstanding, at all times constitutes an obligation of the utility customer of record in respect to the premises served by the measure to repay; and

(C) arrears in repayment of a loan issued under the program that are outstanding prior to sale or transfer of the applicable real property remains the responsibility of the incurring customer, unless expressly assumed by the subsequent customer or third party.

(4.5) For each loan issued under the program, the utility or its agent shall record in the county recorder's office of a county in which the property is located, a notice, with respect to the real property on which the premises served by the measures are located, of the existence of the loan obligation and stating the total amount of the loan obligation, the term of the loan obligation, and that the loan obligation is being repaid through a charge on a gas service provided to the property. The notice shall also state that it is being filed under this Section and, unless fully satisfied prior to sale or transfer of the property, the loan obligation shall survive changes in ownership, tenancy, or meter account responsibility and, until fully satisfied, shall constitute the obligation of the person responsible for the meter account. The notice shall not constitute a mortgage or deed of trust and shall not create any security interest or lien on the property. Upon satisfaction of the loan obligation, the utility or its agent shall promptly record a notice of repayment or a termination of notice. The county recorder shall record the notices in the same book in which the deeds are recorded.

Disconnection for non-payment: YES

Sec. 19-140 (c)(6). In addition, the gas utility shall retain a security interest in the measure or measures purchased under the program, and the utility retains its right to disconnect a participant that defaults on the payment of its utility bill.

Michigan

Spurred by Substitute House Bill 5397 (2014), Holland Board of Public Works – a municipal utility – launched in late 2016 their Holland On-Bill Loan Program, an on-bill financing program for their customers.

S. 438 (2016)

Loan repayment on the bill: YES

Sec. 205(2). Under a residential energy projects program, if a record owner of property in the provider's service territory obtains financing or refinancing of an energy project on the property from a commercial lender or other legal entity, including an independent subsidiary of the provider, the loan is repaid through itemized charges on the provider's utility bill for that property. The itemized charges may cover: the cost of materials and labor necessary for installation, home energy audit costs, permit fees, inspection fees, application and administrative fees, bank fees, and all other fees that may be incurred by the record owner for the installation on a specific or pro rata basis, as determined by the provider.

Sec. 209(1). The term of a loan paid through a residential energy projects program shall not exceed the anticipated useful life of the energy project financed by the loan or 180 months, whichever is less. The loan shall be repaid in monthly installments.

Follows the meter: YES

Disconnection for non-payment: YES

Sec. 209 (2). Electric or natural gas service may be shut off for nonpayment of the per-meter charge described under Sec. 205 in the same manner and pursuant to the same procedures as used to enforce nonpayment of other charges for the provider's electric or natural gas service. If notice of a loan under the program is recorded with the register of 24 ESB 438 deeds for the county in which the property is located, the obligation to pay the per-meter charge shall run with the land and be binding on future customers contracting for electric service or natural gas service, as applicable, to the property.

New York

Launched in 2012, the On-Bill Recovery Finance (OBRF) Loan program, administered by the New York State Energy Research and Development Authority (NYSERDA) is supported by the Power New York Act of 2011, approved by the New York State Legislature.

Green Jobs - Green New York Act (2009)

Sec. 1896 1.(c)(iii). Establish an on-bill recovery mechanism for repayment of loans for the performance of qualified energy efficiency services for eligible projects, provided that such on-bill recovery mechanism shall provide for the utilization of any on-bill recovery programs established pursuant to Sec. 66-m of the public service law and Sec.1,020-hh of this chapter;

Sec. 1896 1.(c)(iv). Establish standards for customer participation in such on-bill recovery mechanism, including standards for reliable utility bill payment, current good standing on any mortgage obligations, and such additional standards as the authority deems necessary; provided that in order to provide broad access to on-bill recovery, the authority shall, to the fullest extent practicable, consider alternative measures of creditworthiness that are prudent in order to include participation by customers who are less likely to have access to traditional sources of financing;…

Sec. 1896 2.(e). In establishing an on-bill recovery mechanism:

(i) the cost-effectiveness of an eligible project shall be evaluated solely on the basis of the costs and projected savings to the applying customer, using standard engineering assessments and prior billing data and usage patterns; provided however, that based upon the most recent customer data available, on an annualized basis, the monthly on-bill repayment amount for a package of measures shall not exceed one-twelfth of the savings projected to result from the installation of the measures provided further that nothing herein shall be construed to prohibit or prevent customers whose primary heating energy source is from deliverable fuels from participating in the program;

(ii) the authority shall establish a process for receipt and resolution of customer complaints concerning on-bill recovery charges and for addressing delays and defaults in customer payments; and

(iii) the authority may limit the availability of lighting measures or household appliances that are not permanently affixed to real property.

Sec. 1896 2.(f). Prior to or at the closing of each loan made pursuant to this section, the authority shall cause a notice to be provided to each customer receiving such loan stating, in clear and conspicuous terms:

(i) the financial and legal obligations and risks of accepting such loan responsibilities, including the obligation to provide or consent to the customer's utility providing the authority information on the sources and quantities of energy used in the customer's premises and any improvements or modifications to the premises, use of the premises or energy consuming appliances or equipment of any type that may significantly affect energy usage;

(ii) that the on-bill recovery charge will be billed by such customer utility company and that failure to pay such on-bill recovery charge may result in the customer having his or her electricity and/or gas terminated for non-payment, provided that such utility company follows the requirements of Article Two of The Public Service Law with respect to residential customers;

(iii) that incurring such loan to undertake energy-efficiency projects may not result in lower monthly energy costs over time, based on additional factors that contribute to monthly energy costs;

(iv) that the program is operated by the authority and it is the sole responsibility of the authority to handle consumer inquiries and complaints related to the operation and lending associated with the program, provided further that the authority shall provide a mechanism to receive such consumer inquiries and complaints.

Sec. 1896 2.(g). Any person entering into a loan agreement pursuant to this section shall have the right to cancel any such loan agreement until midnight of the fifth business day following the day on which such person signs such agreement, provided the loan proceeds have not yet been disbursed.

Sec. 1896 5.(a) For each loan issued for qualified energy efficiency services that is to be repaid through an on-bill recovery mechanism, the New York state energy research and development authority shall record, pursuant to article nine of the Real Property

Law, in the office of the appropriate recording officer, a declaration with respect to the property improved by such services of the existence of the loan and stating the total amount of the loan, the term of the loan, and that the loan is being repaid through a charge on an electric or gas meter associated with the property. The declaration shall further state that it is being filed pursuant to this section and, unless fully satisfied prior to sale or transfer of the property, the loan repayment utility meter charge shall survive changes in ownership, tenancy, or meter account responsibility and, until fully satisfied, shall constitute the obligation of the person responsible for the meter account. Such declaration shall not constitute a mortgage and shall not create any security interest or lien on the property. Upon satisfaction of the loan, the authority shall file a declaration of repayment pursuant to article nine of the Real Property Law.

Power New York Act of 2011

Sec. 66-m 1.(d). The on-bill recovery charge shall be collected on the bill from the customer's electric corporation unless the qualified energy efficiency services at that customer's premises result in more projected energy savings on the customer's gas bill than the electric bill, in which case such charge shall be collected on the customer's gas corporation bill.

Sec. 66-m 2.(d) unless fully satisfied prior to sale or transfer, that (i) the on-bill recovery charges for any services provided at the customer's premises shall survive changes in ownership, tenancy, or meter account responsibility, and (ii) that arrears in on-bill recovery charges at the time of account closure or meter transfer shall remain the responsibility of the incurring customer, unless expressly assumed by a subsequent purchaser of the property subject to such charges;

Sec. 66-m 1.(e) not less than 45 days after closure of an account that is subject to an on-bill recovery charge, and provided that the customer does not re-establish service with such electric and gas corporation, it shall be the responsibility of the New York State Energy Research and Development Authority and not the electric and gas corporation to collect any arrears that are due and owing;

Sec. 66-m 1.(f) a customer remitting less than the total amount due for electric and/or gas services and on-bill recovery charges shall have such partial payment first applied as payment for electric and/or gas services and any remaining amount will be applied to the on-bill recovery charge…

Sec. 11. Section 242 of the Real Property Law is amended by adding a new Subdivision 4 to read as follows:

4. Disclosure prior to the sale of real property to which a green jobs-green New York on-bill recovery charge applies.

(a) Any person, firm, company, partnership or corporation offering to sell real property which is subject to a green jobs-green New York on-bill recovery charge pursuant to Title 9-A of Article 8 of the Public Authorities Law shall provide written notice to the prospective purchaser or the prospective purchaser's agent, stating as follows: "This property is subject to a Green Jobs-Green New York on-bill recovery charge". Such notice shall also state:

the total amount of the original charge, the payment schedule, and the approximate remaining balance; a description of the energy efficiency services performed, including improvements to the property; and an explanation of the benefit of the Green Jobs-Green New York qualified energy efficiency services. Such notice shall be provided by the seller prior to accepting a purchase offer.

(b) Any prospective or actual purchaser who has suffered a loss due to a violation of this subdivision is entitled to recover any actual damages incurred from the person offering to sell or selling said real property.

Oregon

With the passage in 2009 of HAB 2626, The Energy Efficiency and Sustainable Technology Act (EEAST) by Oregon State legislature, NW Natural Gas, Portland General Electric, and Pacific Power –all Investor Owned Utilities (IOU) – set up on-bill repayment program. Clean Energy Works– Oregon, now called Inhabit, manages the statewide program for the utilities using capital from an established loan fund. The loan fund, managed by Enterprise Cascadia, a regional community development financial institution (CDFI), receives capital from the Small Scale Loan Energy project loan Fund (SELP). The program is offered to homeowners and with good credit scores, at least a 590 score.

HB 2626 (2009)

Loan repayments on the customer's utility bill:

Sec. 32 (2). Unless the Public Utility Commission grants an investor-owned utility a waiver under Subsection (4) of this section, the on-bill financing system of the utility must:

(a) Enable a customer to make a single payment to satisfy the periodic utility charges and repayment on an energy efficiency and sustainable technology loan;

(b) Provide a clearly identifiable line item or separate statement in the utility bill that shows the energy efficiency and sustainable technology loan repayment amount;

Disconnection for non-payment:

Sec. 32 (3). The Public Utility Commission shall adopt rules for the use of on-bill financing by investor-owned utilities. The rules may include, but need not be limited to, rules regarding: nonpayment, insufficient payment, and delinquency notices; repayment charge transfers; processing fees; late fees; and refunds. The commission may not adopt any rule that imposes responsibility for the repayment of an energy efficiency and sustainable technology loan on the utility.

Follows the meter:

Sec. 64 (7). If the project is being financed by an energy efficiency and sustainable technology loan or small scale local energy program loan, in addition to the requirements of Subsections (1) to (6) of this section, shall include:

(a) For an energy efficiency and sustainable technology loan that relies on an on-bill financing system for the collection of a loan repayment charge, an agreement by the applicant to notify a person acquiring ownership of, or an interest in, the property from the applicant that the loan re-payment charge will be transferred to the utility customer account of the person acquiring the ownership or interest unless the loan is discharged before or at the time the ownership or interest transfers;

(b) A plainly worded acknowledgment by the applicant that failure to make payments as required under the loan agreement may result in the foreclosure of a property lien or other debt collection actions;

(c) A waiver stating that the applicant waives any jurisdictional or other irregularities or defects in:

(A) The energy efficiency and sustainable technology loan program;

(B) A small scale local energy project;

(C) The small scale local energy program loan provisions;

(D) This chapter; or

(E) Department rules that relate in any way to the loan repayment charge, real property lien provisions, or any form or combination of loan security or to the requirement to satisfy the loan obligation;

(d) If the applicant is not the owner of the property to be burdened by the loan repayment charge, fixture filing or real property lien, provision for participation by the property owner as a party to the contract or a notarized authorization by the owner for the fixture filing and lien; and

(e) A description of any other conditions required by the department.

South Carolina

Since 2011, the Help My House Program, supported by state legislation, has been run by the Electric Cooperatives of South Carolina.

S 1096 (2010)

Loan repayments on the customer's utility bill.

Disconnection for non-payment:

S 1096(B). Electricity providers and natural gas providers may enter into written agreements with customers and landlords of customers for the financing of the purchase price and installation costs of energy efficiency and conservation measures. These agreements may provide that the costs must be recovered by a meter conservation charge on the customer's electricity or natural gas account, provided that the electricity providers and natural gas providers comply with the provisions of this section. A failure to pay the meter conservation charge may be treated by the electricity provider or natural gas provider as a failure to pay the electricity or natural gas account, and the electricity provider or natural gas provider may disconnect electricity or natural gas service for nonpayment of the meter conservation charge, provided the electricity

provider or natural gas provider complies with the provisions of: Article 25, Chapter 31, Title 5; Article 17, Chapter 11, Title 6; Article 17, Chapter 49, Title 33; Article 11, Chapter 5, Title 58; Article 21, Chapter 27, Title 58; Article 5, Chapter 31, Title 58; and any applicable rules, regulations, or ordinances relating to disconnections.

S 1096(D). An electricity provider or natural gas provider may recover the costs, including financing costs, of these measures from its members or customers directly benefiting from the installation of the energy efficiency and conservation measures. Recovery may be through a meter conservation charge to the account of the member or customer and any such charge must be shown by a separate line item on the account.

Loan follows the meter:

S 1096(G). An electricity provider or natural gas provider that enters into an agreement as pro-vided in this section may recover the costs, including financing costs, of energy efficiency and conservation measures from subsequent purchasers of the residence in which the measures are installed, provided the electricity provider or natural gas provider gives record notice that the residence is subject to the agreement. Notice must be given, at the expense of the filer, by filing a notice of meter conservation charge with the appropriate office for the county in which the residence is located, pursuant to Section 30-5-10. The notice of meter conservation charge does not constitute a lien on the property but is intended to give a purchaser of the residence notice that the residence is subject to a meter conservation charge. Notice is deemed to have been given if a search of the property records of the county discloses the existence of the charge and informs a prospective purchaser: (1) how to ascertain the amount of the charge and the length of time it is expected to remain in effect, and (2) of his obligation to notify a tenant if the purchaser leases the property as provided in Subsection (H)(3).