

Department of Legislative Services
Maryland General Assembly
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FISCAL NOTE

Senate Bill 557 (Senator Frosh. *et al.*)

Finance

Consumer Protection and Electric Utility Restructuring Act of 1999

This bill generally provides for the restructuring of the electric utility industry in Maryland, subject to the oversight of the Public Service Commission (PSC).

Fiscal Summary

State Effect: Public Service Commission general fund expenditures could increase by approximately \$60,000 annually. The Office of the Attorney General general fund expenditures could increase by approximately \$173,000 annually. Indeterminate increase in Maryland Energy Administration general fund expenditures. Potential increase in corporate income tax revenues. Special fund revenues and expenditures could increase by \$173,443,400 for the newly established Public Benefits Fund. Indeterminate effect on the State as a consumer of electricity. The Office of the People's Counsel and the Maryland Department of the Environment could handle the bill's requirements with existing resources.

Local Effect: Potential meaningful effect on local governments as "aggregators" of electricity consumers. Potential increase in tax revenues. Indeterminate effect on local governments as consumers of electricity.

Small Business Effect: Potential meaningful opportunity for small businesses to enter the electric utility industry. Indeterminate effect on small businesses as consumers of electricity.

Fiscal Analysis

Bill Summary: This bill generally provides for the restructuring of the electric utility industry in Maryland, subject to the oversight of the Public Service Commission. The primary provisions of the bill are summarized below.

- The bill's provisions are contingent on the enactment of related tax legislation.
- The bill overturns a PSC order to begin electric utility deregulation in July 2000.
- The bill prohibits the implementation of retail choice unless the PSC: (1) determines in a written order that sufficient local, regional, and national reliability organizations and systems are in place; (2) determines in a written order that control systems necessary for operating an interconnected transmission grid in a competitive market exist; (3) determines that there is an independent means to operate and manage the bulk power system on a regional basis for reliability purposes; (4) determines that all customer classes will obtain economic benefits from electric restructuring; (5) has promulgated specified regulations (i.e., consumer protections, billing requirements, basic service offers, anti-competitive conduct, supplier licensure); and (6) has determined the value of the stranded costs or benefits.
- Each utility must arrange for basic service for residential and small commercial consumers who choose the basic service option, are not yet eligible for an energy service provider or buyer aggregator, or have been denied service by a retail electric provider. Basic electric service is defined as the same services which were provided to residential customers under the PSC-approved residential service tariff in effect prior to retail access.
- The PSC must establish requirements for entities to qualify as a buyers aggregator, to establish reasonable consumer protection requirements for buyers aggregators, to assist groups that wish to become buyers aggregators to understand the technical and economic issues in buying electric supply in a competitive market, and to establish regulations relating to buyers aggregator.
- Sellers, marketers, brokers, and aggregators must obtain a retail electric service provider license from the PSC. The bill authorizes the PSC to collect a fee and to promulgate bonding or insurance regulations. The bill requires a licensee to comply with the Federal Energy Regulatory Commission's orders and regulations and to have the technical, managerial, and financial capability to provide energy services in Maryland.

- The bill establishes a Public Benefits Fund in the Maryland Energy Administration (MEA) to provide funding for the development of renewable energy resources, energy efficiency programs, universal service programs, and assistance for small customers to form buyer aggregators. A minimum of 5% of the fund must be used for renewable energy programs; a minimum of 30% must be used for energy efficiency programs; and a minimum of 40% must be used for low-income programs. For three years after the commencement of retail access, up to \$500,000 annually must be used to assist small customers aggregate. The bill requires .3 cents on each kilowatt-hour to be placed in the Public Benefits Fund.
- MEA must develop a renewable energy program, an energy efficiency program, and a program to assist small customers in becoming buyer aggregators. MEA is also required to convene a Low-Income Energy Assistance Advisory Board.
- The bill caps electric rates to retail consumers for four years following the initial implementation of consumer choice. This cap may not exceed the cost of service regulated rates per customer class for those services on a bundled basis before retail access.
- The bill requires an investor-owned electric utility to apply to the PSC for a determination of the recovery of stranded costs. An electric utility may not claim stranded costs unless it has submitted all of its generation assets, except for nuclear assets, to a public auction. An affiliate or subsidiary may bid on the assets. The PSC must use the results of the auction to determine the stranded costs or benefits relating to generation. A utility may recover its stranded costs based on specified factors such as the prudence of the original investment. A utility must credit stranded benefits to the ratepayers. Generation assets not sold will be transferred at book value to an affiliate or subsidiary.
- A municipal electric company or a rural electric cooperative may not be required to make its service territory available to retail competition unless it elects to do so. If such a company elects not to allow retail choice within its service area, it may not compete outside its service area.
- The bill allows a county within six months of retail access to choose to act as a buyers aggregator. If a county has not acted within six months, a municipal corporation may act as a buyers aggregator. If a municipal corporation has not acted within one year, any other legally authorized person may act as a buyers aggregator.
- The bill extends the termination date of the environmental surcharge that is paid by electric companies from fiscal 2000 to fiscal 2005, and requires .015 cents on each

kilowatt-hour of electricity delivered in the State to be remitted to the Comptroller and placed in the Environmental Trust Fund.

- For emissions of oxides of nitrogen into the air, the bill requires retail power sellers to meet or exceed .15 pounds per million BTU. For sulfur dioxide air emissions, the seller must meet or exceed 1.2 pounds per million BTU.
- The PSC must monitor the markets for electric services to identify and prevent any conduct that impedes the development of fully competitive markets. If the PSC finds that anti-competitive behavior has occurred or an anti-competitive condition exists, the PSC may impose any appropriate structural or behavioral remedy.
- The PSC is required, in consultation with the Division of Consumer Protection of the Office of the Attorney General, to adopt regulations that provide specified consumer protections (i.e., uniform disclosure, restrictions on telemarketing, procedures for customer enrollment, billing and collection requirements, prohibition on the disconnection of electric service, dispute resolution procedures). The PSC must cooperate with the Attorney General to enforce all applicable consumer protection laws.

State Effect: This bill would affect the State administratively and as a consumer of electricity. The bill could also cause an indeterminate increase in general fund revenues resulting from taxes collected on the sale of generation assets. It is unclear whether utility rates charged to the State will increase or decrease in the future, as discussed in the Small Business section of this fiscal note.

The Public Service Commission and the Office of the People's Counsel (OPC): The bill generally provides for the restructuring of the electric utility industry in Maryland, subject to PSC oversight. The PSC has already issued several orders setting forth plans for retail electric competition beginning in July 2000. This bill clarifies the PSC's authority to proceed with deregulation. The OPC advises that it could handle the bill's requirements with existing resources, and the PSC advises that it could handle the majority of the bill's requirements with existing budgeted resources.

The bill requires the PSC to establish requirements for entities to qualify as a buyers aggregator, to establish reasonable consumer protection requirements for buyers aggregators, to assist groups that seek to become buyers aggregators to understand the technical and economic issues in buying electric supply in a competitive market, and to establish regulations relating to buyers aggregators. The PSC would need to hire one regulatory economist II to manage the aggregation assistance aspects of the bill at an annualized cost of about \$60,000.

It should be noted that under §2-110 of the Public Utility Companies Article, the PSC and the OPC may assess each “public service company” .17% and .05% of the company’s gross operating revenue derived from intrastate competition utility to fund the PSC and the OPC, respectively. However, “retail electric service providers” (i.e., marketers, brokers) are not “public service companies” and therefore not subject to PSC and OPC assessments. Thus, because these electricity suppliers are not a part of the general revenue against which assessments may be applied, PSC and OPC funding may decline. However, the PSC advises that it is currently assessing public utility companies at a rate of .1659%. As a result, the PSC’s operating budget would not be affected unless public service company operating revenues declined more than \$1.8 billion as a result of this bill.

Maryland Department of the Environment (MDE): Any additional workload to MDE resulting from this bill could be handled with existing resources. The bill requires the PSC, in consultation with the MDE, to adopt appropriate measures to maintain environmental safeguards, continue existing programs, and develop new programs as appropriate to ensure that federal and State environmental protection standards are not compromised in a competitive electricity market. The bill also requires the PSC, in consultation with the MDE to conduct proceedings to establish standards and procedures to implement the disclosure requirements of fuel mix and emissions to consumers. These provisions do not substantially alter MDE’s responsibilities regarding environmental regulation of electric utilities.

Maryland Energy Administration (MEA): The bill would have a significant effect on the operations and finances of the MEA. The bill establishes a Public Benefits Fund to provide funding for the development of renewable energy resources, energy efficiency programs, universal service programs, and assistance for small customers to form as buyers aggregator. The bill requires ratepayers to contribute .3 cents on each kilowatt-hour to the Public Benefits Funds. In 1998 Maryland consumed 57,814,465,000 kilowatts of electricity. Therefore, the Public Benefits Fund is expected to generate \$173,443,400 annually. At least 5% must be used for renewable energy programs; at least 30% must be used for energy efficiency programs; and at least 40% must be used for low-income programs. For three years after the commencement of retail access, up to \$500,000 annually must be used to assist small customers aggregate. The Maryland Energy Administration must establish the annual

budgets for the renewable energy programs, energy efficiency programs, universal service programs, and aggregation for small customers. The bill also requires MEA to develop a renewable energy program, an energy efficiency program, and a program to assist small customers in becoming buyer aggregators. Moreover, MEA is required to convene a Low-Income Energy Assistance Advisory Board. MEA would require additional staff and operating costs. However, the Department of Legislative Services (DLS) cannot provide an accurate estimate of these costs without further information from MEA.

Office of the Attorney General (OAG): The PSC is required, in consultation with the Division of Consumer Protection of the Office of the Attorney General, to adopt regulations that provide specified consumer protections (i.e., uniform disclosure, restriction on telemarketing, procedures for customer enrollment, billing and collection requirements, prohibition on the disconnection of electric service, dispute resolution procedures). The PSC is required to cooperate with the Attorney General in enforcement of all applicable consumer protection laws. The OAG advises that it would need to hire an assistant attorney general, a fraud investigator, and a complaint supervisor to handle these additional responsibilities, resulting in a general fund expenditure increase of approximately \$173,000 on an annual basis.

Department of Natural Resources (DNR): The bill extends the termination date of the environmental surcharge that is paid by electric companies from fiscal 2000 to fiscal 2005, and continues to require .015 cents on each kilowatt-hour of electricity delivered in the State to be remitted to the Comptroller and placed in the Environmental Trust Fund. The trust fund is used to support activities associated with the assessment and management of cultural, economic, and environmental effects of electric power and electric power facilities on the State. These activities are coordinated through the Power Plant Research Program of DNR. In fiscal 1998 trust fund revenues totaled \$8.2 million, of which \$6.9 million came from the environmental surcharge. Expenditures for fiscal 1998 were \$7.7 million.

Indeterminate increase in tax revenues: An electric utility may not claim stranded costs unless it has submitted all of its non-nuclear generation assets to a public auction before July 1, 2000. In October 1998 transition costs filings totaling \$1.9 billion were made by the utilities. To the extent that assets are sold at auction as a result of the bill, the State would collect additional taxes on the income earned from the sale. The amount of the additional income realized by the utility companies and the corporation income tax revenues collected by the State will depend on the auction price and any tax legislation that is passed related to deregulation. Approximately 25% of the corporate income tax is distributed to the Transportation Trust Fund. In addition, there are transfer and recordation taxes associated with each sale.

Local Effect: This bill provides local governments an opportunity to act as "aggregators" of

utility consumers. Moreover, local governments could realize additional tax revenues and would be affected as consumers of electricity. It is unclear whether utility rates charged to these governments will increase or decrease in the future, as discussed in the Small Business section of this fiscal note.

This bill gives local governments and municipalities the first chance to act as buyers aggregators. The bill allows a county within six months of retail access to choose to act as a buyers aggregator. If a county has not acted within six months, a municipal corporation may act as a buyers aggregator. If a municipal corporation has not acted within one year, any other legally authorized person may act as a buyers aggregator.

The bill provides that a municipal electric company or a rural electric cooperative may not be required to make available its service territory to retail competition unless it elects to do so. A company that elects not to allow retail access may not market or sell electricity to customers outside its service territory; whereas companies that allow retail access may provide service outside of its service territory.

Local governments could realize additional revenues from taxes collected as a result of this bill. An electric utility may not claim stranded costs unless it has submitted all of its non-nuclear generation assets to a public auction before July 1, 2000. To the extent that there are additional sales of generation assets, local revenues would increase due to local transfer taxes and recordation taxes. Additionally, approximately 25% of any increased State revenue resulting from increased corporate income tax collections would be deposited in the Transportation Trust Fund, a portion of which goes to local governments.

Small Business Effect: This bill has two primary effects on small business finances. First, the electric utility rates paid by small businesses could change in the long run under a deregulated environment. Second, deregulation could provide additional business opportunities for small businesses seeking to enter the electric utility industry.

Small businesses as consumers of electricity: The bill caps total electric rates to small businesses for four years following the initial implementation of customer choice and allows these businesses to shop for lower generation rates. The bill provides that small business consumers who do not wish to change their electricity provider or who are not eligible to choose their electricity provider will receive “basic electric service.” As a result, the bill could result in lower electric utility bills for small businesses during this period. However, once the four-year cap has expired, rates for generation are subject to market forces.

In the long run, it is unclear whether rates will increase or decrease for small business consumers of electricity. This determination is largely contingent on the value assigned to “stranded costs,” which refers to the difference between the book value of a utility asset and

the market value. Under a regulated environment, rates are set in an administrative rate-making proceeding to allow companies an opportunity to recover their operating expenses, depreciation expenses, and a reasonable rate of return. Because rates are cost-based, there are no stranded costs. However, in a competitive environment, the market may cause prices to decline and thus cause the rate of return on existing assets to also decline. Stranded costs arise when the electric utility cannot recover an asset's fixed costs out of the market price of electricity. One of the most difficult tasks that regulators have confronted in promoting competition in the electric power industry has been determining how to measure these stranded costs.

The bill requires an investor-owned electric company to apply to the PSC for a determination of the recovery of stranded costs. However, an electric utility may not claim stranded costs unless it has submitted all of its generation assets, except for nuclear assets, to a public auction. An affiliate or subsidiary may bid on the assets. The PSC must use the results of the auction to determine the stranded costs or benefits relating to generation. A utility may recover its stranded costs based on specified factors such as the prudence of the original investment. A utility must credit stranded benefits to the ratepayers. Generation assets not sold will be transferred at book value to an affiliate or subsidiary.

Given that the primary obstacle to valuing stranded costs is determining the market value of the assets, this bill requires utilities to sell their generating assets. Assuming that the auction produces a fair market value for the assets and the stranded costs are accurately valued, electric utility rates to small business consumers should not increase as a result of stranded costs. However, to the extent that the auction does not create perfectly competitive market conditions (i.e., small number of bidders, large blocks of assets are not easily sold), the price offered by the highest bidder may be less than the market value causing the stranded costs to be overvalued.

The bill also continues to require each customer to pay .015 cents on each kilowatt-hour of electricity to be deposited in the Environmental Trust Fund. Furthermore, the bill requires .3 cents on each kilowatt-hour to be placed in the Public Benefits Fund. As a result, small businesses would pay slightly higher electric rates.

Despite the increase in rates due to contributions to the Public Benefits Fund and the indeterminate effect of stranded costs on rates, small business consumers of electricity could benefit from deregulation, as competition will encourage innovation and efficiency in the industry that could result in downward pressure on price. Furthermore, the bill provides for the "aggregation" of individuals or entities that act on behalf of a customer to purchase electricity. As result, small businesses may "aggregate" with other consumers of electricity to increase their bargaining position in contracting for utility rates.

Potential Business Opportunity for Small Businesses to Enter Electric Utility Industry:

Under a regulated electric utility environment, only public service companies may supply electricity. This bill would allow small businesses to enter the electric utility industry as brokers, marketers, or billing service providers. Of course, any small business that entered the market would have to comply with the bill's licensing requirements.

Information Sources: Public Service Commission, Maryland Department of the Environment, Attorney General's Office, Maryland Energy Administration, Department of Assessments and Taxation

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