Department of Legislative Services

Maryland General Assembly
2000 Session

FISCAL NOTE

House Bill 741 (Delegate Sher)
Ways and Means

State Income Tax Credit for Competitive Transition Charges Paid for On-Site Generated Electricity

This bill allows a credit against the State income tax in the amount of 100% of competitive transition charges paid to an electric company in the State for on-site generated electricity at a facility that combines heating and power output with an energy efficiency of at least 70%.

The bill takes effect July 1, 2000, and applies to all taxable years beginning after December 31, 1999.

Fiscal Summary

State Effect: General fund revenue loss of approximately $1.04 million and Transportation Trust Fund (TTF) revenue loss of approximately $243,700 in FY 2001. Future year losses reflect additional self-generation megawatt hours and a four-year competitive transition charge. No effect on expenditures.

(in millions)	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005
GF Revenues	($1.04)	($2.09)	($3.13)	($4.18)	
SF Revenues	($0.244)	($0.487)	($0.731)	($0.975)	
GF Expenditures	$0.0	$0.0	$0.0	$0.0	
Net Effect	($1.284)	($2.577)	($3.861)	($5.155)	

Note: ( ) = decrease; GF = general funds; FF = federal funds; SF = special funds; - =indeterminate effect

Local Effect: Local government revenue loss of approximately $104,400 in FY 2001.

Small Business Effect: Potential meaningful. To the extent that small businesses are able to generate their own power, they would be able to claim the credit against competitive transition charges paid.

Analysis

Current Law: A competitive transition charge is a rate, charge, credit, or other appropriate mechanism authorized to be imposed for the recovery of transition costs. A competitive transition charge as determined by the Public Service Commission may be imposed on customers who access the transmission or distribution system of the electric company in whose distribution territory the customer is located. The cost authorized by the commission to be recovered shall be allocated to customer classes in a manner that, as nearly as reasonably possible, does not exceed the cost of providing the service to those classes of customers, avoiding where reasonably possible any interclass or interclass cross subsidy.

No credit exists for competitive transition charges paid.

Background: After several years of debate in the legislature and in regulatory circles, the General Assembly enacted legislation to restructure the electric utility industry in Maryland. Chapters 3 and 4 of 1999 phased in customer choice for all investor-owned utility customers between 2000 and 2002, together with customer protections, a new universal service program for low-income customers, and environmental protections that address a restructured electric framework.

To date, 18 states have chosen to deregulate with legislation and several others have regulations in place. As a result, there is pressure on the remaining states to allow their locally-based utilities and businesses to compete and benefit from a deregulated electricity generation market. Maryland's neighbors, Pennsylvania, Delaware, New Jersey, and Virginia, have each enacted legislation on this issue.

One of the most complex issues in enacting electric utility industry restructuring has been the issue of how to treat transition costs or benefits. The term “transition costs” 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 transition costs. However, in a competitive environment, the market may cause prices to decline and thus cause the rate of return on existing assets also to decline. Transition 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 transition costs.

Although Chapters 3 and 4 may allow an electric company an opportunity to recover certain prudently incurred transition costs, it may only do so under a commission-approved transition plan, developed in accordance with fact-finding and evidentiary proceedings, and subject to full mitigation.

If approved by the commission, an electric company with verified recoverable transition costs may institute a competitive transition charge that applies generally to customers located in the electric company's service territory. There is an exemption for customers with on-site electric generation under certain circumstances.

Under the Acts, an electric company may transfer any of its generation facilities or generation assets to an affiliate, but the transfer may not affect or restrict the commission's determination of the value of a generation asset for purposes of transition costs or benefits.

Under current law, there is no per kilowatt hour tax on the self-generation of electricity, nor is it subject to the 2% gross receipts tax on distribution services (other than the competitive transition charge). Also, self-generation is exempt from the 5% sales and use tax imposed on commercial customers.

State Fiscal Effect: The Public Service Commission has determined that Baltimore Gas and Electric (BGE) can recover approximately $528 million in transition charges. In order to recover this money, BGE will add a competitive transition charge (CTC) to each customer's bill. The CTC is $.00742 per kilowatt hour. BGE is the only electric utility currently projected to have a CTC. According to BGE, there are currently three projects in its service area that would qualify for the credit for self-generated power proposed by the bill. The three projects have a total of 25.5 megawatt hours capacity. At a CTC of $.00742 per kilowatt hour, an estimated $1.04 million would be lost each year for the credit.

Assuming that an additional 25.5 megawatt hours will be lost to self-generation each year and a CTC of $.00742 per kilowatt hour, approximately $14 million will be lost over the four-year recovery period. All the customers are assumed to be corporate entities, and that the credit would not exceed the State tax liability. Credits are assumed to reduce revenue in the fiscal year following the year that returns are filed. Because 75% of all corporate income tax revenues are distributed to the general fund and 25% are distributed to the TTF, credits taken on corporate income tax returns will reduce general fund revenues by 75% of the amount of the credits taken, and TTF revenues will be reduced by 25% of the credits taken. In addition, 30% of the 25% of revenue distributed to the TTF is distributed to local governments.

Tax Year	Self-Generation Megawatt Hours	Cost	General Fund	TTF	Local

TY 2000	25.5	$1,392,608	$1,044,456	$243,706	$104,446
TY 2001	51.0	$2,785,216	$2,088,912	$487,413	$208,891
TY 2002	76.5	$4,177,824	$3,133,368	$731,119	$313,337
TY 2003	102.0	$5,570,431	$4,177,824	$974,826	$417,782
Total	**255.0**	**$13,926,079**	**$10,444,560**	**$2,437,064**	**$1,044,456**

Local Fiscal Effect: Local government revenues would decline as a result of corporate taxpayers claiming the credits proposed in the bill. As mentioned above, 75% of corporate tax revenues are distributed to the general fund, and 25% are distributed to the TTF. Of the 25% distributed to the TTF, approximately 30% is distributed to local jurisdictions. Based on the above estimate, local government revenues would decline by approximately $104,400 in fiscal 2001.

Additional Information

Prior Introductions: None.

Cross File: SB 622 (Senator Teitelbaum) - Budget and Taxation.

Information Source(s): Comptroller of the Treasury (Bureau of Revenue Estimates), Public Service Commission, Baltimore Gas and Electric, Department of Legislative Services

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