

Department of Legislative Services
Maryland General Assembly
2015 Session

FISCAL AND POLICY NOTE

House Bill 1043 (Delegate Parrott, *et al.*)
Environment and Transportation

**Environment - On-Site Sewage Disposal System - Nitrogen Removal Technology
- Exemption**

This bill authorizes a person to install a new onsite sewage disposal (septic) system, or replace an existing septic system, on property outside of the Chesapeake and Atlantic Coastal Bays Critical Area without the use of nitrogen removal technology. Regulations of the Maryland Department of the Environment (MDE) may not require a new or replacement septic system to use nitrogen removal technology on property outside of the Critical Area.

Fiscal Summary

State Effect: General fund revenues increase, potentially by more than \$100,000 annually, beginning in FY 2016 from fewer subtraction modification claims against personal income taxes from individuals installing septic systems that utilize nitrogen removal technology. State expenditures (all funds) may increase to implement other nutrient reduction strategies necessary to achieve State and federal Chesapeake Bay restoration mandates, partially offset by lower costs for State projects involving the installation of septic systems.

Local Effect: Local income tax revenues increase minimally from fewer subtraction modification claims against personal income taxes. Local revenues also decrease for some jurisdictions that receive fewer Bay Restoration Fund (BRF) administrative grants associated with the upgrade of septic systems, although other jurisdictions with a greater number of septic systems within the Critical Area may receive greater funds. Local workloads related to inspection and enforcement of septic systems that utilize nitrogen removal technology decrease for certain jurisdictions. Local expenditures decrease minimally as costs decrease for some local projects served by septic systems.

Small Business Effect: Potential meaningful.

Analysis

Current Law: Chapter 280 of 2009 prohibits a person from newly installing or replacing a septic system on property in the Critical Area unless the installed system utilizes best available technology (BAT) for nitrogen removal. MDE is required to assist homeowners in upgrading a septic system with money authorized for this purpose from the BRF Septics Account, if sufficient funds are available. In addition, Chapter 280 of 2009 created a subtraction modification against the personal income tax for the cost of upgrading a septic system, less any assistance provided.

Priority for funding from the Septics Account is as follows: (1) failing systems in the Critical Area; (2) other failing systems; (3) new or replacement systems in the Critical Area; and (4) other new or replacement systems.

In September 2012, MDE adopted regulations, effective January 1, 2013, that expanded the required use of BAT septic systems to apply to systems serving new construction (but not replacement systems) in any nitrogen impaired waterbody in the State. Because the Chesapeake Bay is impaired by nitrogen, this requirement applies to the entire portion of the Chesapeake Bay watershed in Maryland, which is the vast majority of the State.

Chapter 379 of 2014 requires up to 10% of the funds in the Septics Account to be distributed to a local public entity to cover reasonable costs associated with the implementation of MDE regulations pertaining to upgraded septic systems. The grants were designed to compensate local health departments and other delegated entities for the increasing workloads caused by the phase-out in 2010 of the State's administration of the septic system upgrade program, as well as the additional burden imposed by the new regulations.

Background: Chapter 428 of 2004 established BRF, which is administered by the Water Quality Financing Administration within MDE. The main goal of BRF is to provide grants to owners of wastewater treatment plants (WWTPs) to reduce nutrient pollution to the Chesapeake Bay by upgrading the systems with enhanced nutrient removal (ENR) technology. The fund is also used to support septic system upgrades and the planting of cover crops.

As a revenue source for the fund, Chapter 428 established a bay restoration fee on users of wastewater facilities, septic systems, and sewage holding tanks, and Chapter 150 of 2012 doubled the fee for most users. The BRF statute enumerates several uses of fee revenues, including for ENR upgrades of WWTPs, BAT upgrades of septic systems, and funding for Maryland Department of Agriculture (MDA) cover crop activities.

According to the Comptroller's Office, through February 28, 2015, a total of \$692.3 million in bay restoration fees collected from wastewater facility users had been deposited in MDE's Wastewater Account. In addition, of the fee revenues collected from users of septic systems and sewage holding tanks, \$97.3 million had been deposited in MDE's Septics Account, and \$73.6 million had been provided to MDA to support the planting of cover crops.

According to the Maryland Department of Planning (MDP), a house on a septic system causes 6 to 10 times as much nitrogen pollution as a house on public sewer and, without current restrictions on the installation of septic systems to serve new residential development (established by Chapter 149 of 2012), MDP projects that future septic systems could account for three-fourths of new nitrogen pollution in Maryland over the next 25 years.

In December 2010, the U.S Environmental Protection Agency (EPA) established the Total Maximum Daily Load for the Chesapeake Bay (bay TMDL), which (1) sets the maximum amount of pollution the bay can receive and still attain water quality standards and (2) identifies specific pollution reduction requirements. The State's Phase II Watershed Implementation Plan (WIP) to meet the bay TMDL plans for a 38.3% reduction in nitrogen loads from septic systems in the State, which represents nearly one-tenth of the total nitrogen load reductions from all sectors under the plan. To meet this goal, the Phase II WIP established a target of upgrading 43,181 septic systems between 2010 and 2017, although the State's interim milestones goals have been more modest. The State met its 2012-2013 milestone goal of upgrading 1,200 septic systems with BAT, and this goal doubles to 2,400 upgrades for the 2014-2015 milestones; as of February 2015, BRF has supported the installation of more than 7,200 BAT systems.

MDE estimates that – based on the difference in nitrogen pollution between a conventional and BAT septic system for new construction alone – the bill may result in a future increase in nitrogen loading to groundwater of about 28,750 pounds per year and between 8,750 and 14,375 pounds per year to surface waters.

State Revenues: General fund revenues increase beginning in fiscal 2016 due to a decrease in the number of subtraction modifications claimed against the taxable income of homeowners that would otherwise be required to install a BAT septic system, but are not required to under the bill. A reliable estimate of this increase cannot be made due to numerous sources of uncertainty. However, according to data from the Comptroller's Office, the total general fund loss associated with this subtraction modification ranged from about \$194,000 and \$550,000 annually between fiscal 2010 and 2013, with an annual average of roughly \$300,000. A portion of this general fund loss, however, represents properties within the Critical Area, which are unaffected by the bill. Overall, the reduction in subtraction modifications may result in a general fund increase of between \$50,000 and

\$500,000 annually, assuming a continuation in current trends for this subtraction modification.

State Expenditures: The installation of BAT systems is a key strategy within the State's Phase II WIP as approved by EPA for meeting the nutrient reduction targets of the bay TMDL. Thus, the bill may necessitate additional State expenditures associated with other required nutrient reduction measures. However, any additional expenditures associated with a reprioritization of the State's Phase II (or future Phase III) WIP is unlikely to be significant in the short term, because as noted above, septic system upgrades and connections are a relatively small component of the WIP.

To the extent that State agencies have facilities that may otherwise have been required to install a BAT septic system in the future, State expenditures decrease.

Finally, it should be noted that overall BRF finances are not affected, as the bill likely results in only a change in the purpose of grants made from the BRF Septics Account, but not in a reduction in expenditures, assuming the Septics Account generally remains fully subscribed.

Local Revenues: Local government revenues from BRF administrative cost recovery grants decrease significantly (and are potentially eliminated) for some jurisdictions with relatively few septic systems in the Critical Area (*e.g.* Frederick, Howard, Montgomery, and Prince George's counties), but may increase for some jurisdictions with a greater number of septic systems in the Critical Area (*e.g.* Anne Arundel, Calvert, Queen Anne's, and St. Mary's counties). As noted above, Chapter 379 of 2014 authorized up to 10% of the annual funds received by the Septics Account to be disbursed for administrative cost recovery by local jurisdictions. Thus, the bill may significantly reduce the grants provided to counties with little or no land in the Critical Area. Any *overall* reduction in BRF administrative cost recovery grants provided to local governments results in a corresponding increase in the amount of grant funds available for septic system upgrades.

Local income tax revenues also increase as a result of the reduction in subtraction modifications claimed, as discussed above. However, the increase for any single jurisdiction is minimal.

Local Expenditures: Local government workloads decrease for oversight of BAT system installation and operation and maintenance (O&M), which are generally more complex than for conventional systems. Further, enforcement workloads decrease in future years to the extent that noncompliance with O&M requirements associated with BAT septic systems decreases. Finally, to the extent that local agencies have facilities that may otherwise have been required to install a BAT septic system in the future, installation and O&M costs decrease.

Small Business Effect: The bill may result in a meaningful benefit for vendors that derive a relatively significant share of their sales or installation services from conventional septic systems. However, the bill may also result in a meaningful decrease in sales for vendors with a competitive advantage in the sale or installation of BAT systems. Additionally, developers with a relatively significant reliance on development with septic systems may realize a meaningfully beneficial savings in development costs due to the reduced cost of septic system installation. Small businesses generally may realize a meaningful savings in expansion costs as a result of the bill's changes. Finally, small businesses engaged in providing O&M services for BAT systems may realize a meaningful decrease in the demand for their services.

Additional Comments: It is unclear whether the bill, as drafted, invalidates current MDE regulations that require the use of BAT septic systems serving new construction located within the watershed of a nitrogen-impaired waterbody. The regulations that established this requirement were authorized by several other provisions of law in the Environment Article. However, portions of the regulations are rendered obsolete as they appear to be in conflict with the bill's clear authorization to use conventional septic systems in areas outside of the Critical Area.

Additional Information

Prior Introductions: A similar bill, SB 973 of 2013, received an unfavorable report from the Senate Education, Health, and Environmental Affairs Committee. Other similar bills, SB 13 of the 2012 second special session and SB 1305 of the 2012 first special session, were referred to the Senate Rules Committee, but no further action was taken on either bill.

Cross File: None.

Information Source(s): Maryland Department of the Environment, Comptroller's Office, Maryland Department of Planning, Department of Legislative Services

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md/lgc

Analysis by: Evan M. Isaacson

Direct Inquiries to:
(410) 946-5510
(301) 970-5510