

Department of Legislative Services
 Maryland General Assembly
 2015 Session

FISCAL AND POLICY NOTE

House Bill 886 (Delegate Moon, *et al.*)
 Environment and Transportation

Bay Tax Equity Act

This bill establishes a chicken manure pollution fee paid by poultry integrators of \$0.05 for each chicken provided by a poultry integrator to a farmer in the State, beginning October 1, 2015. The fee revenue is used by the Maryland Department of Agriculture (MDA) to fund cover crop activities on agricultural lands upon which chicken manure has been applied as fertilizer. The bill also repeals the current distribution to MDA of a portion of bay restoration fees collected from users of septic systems and sewage holding tanks which is used to fund cover crop activities.

The bill takes effect July 1, 2015.

Fiscal Summary

State Effect: Special fund revenues increase by \$11.3 million in FY 2016 and by \$15.0 million annually thereafter due to the chicken manure pollution fee. Net special fund expenditures increase by at least \$6.3 million annually beginning in FY 2016, which reflects an increase of \$11.2 million annually in spending by the Maryland Department of the Environment (MDE) for the Septic System Upgrade Program and an overall decrease in spending on cover crops by MDA (of \$4.9 million in FY 2016 and at least \$4.6 million annually thereafter).

| (\$ in millions) | FY 2016 | FY 2017 | FY 2018 | FY 2019 | FY 2020 |
|------------------|---------|---------|---------|---------|---------|
| SF Revenue | \$11.3 | \$15.0 | \$15.0 | \$15.0 | \$15.0 |
| SF Expenditure | \$6.3 | \$6.4 | \$6.4 | \$6.5 | \$6.6 |
| Net Effect | \$5.0 | \$8.6 | \$8.6 | \$8.5 | \$8.4 |

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

Local Effect: Local government revenues and expenditures increase by at least \$10.3 million annually for regulation compliance and septic system upgrade grants.

Small Business Effect: Meaningful.

Analysis

Bill Summary: Beginning October 1, 2015, a chicken manure pollution fee must be paid to the Comptroller by a poultry integrator in a manner determined by the Comptroller. The fee is \$0.05 for each chicken a poultry integrator provides to a farmer in the State. The cost of the fee may not be recovered by a poultry integrator from a farmer that raises chickens for the poultry integrator. The revenue from the fee is transferred to the Maryland Agriculture Water Quality Cost Share Program (MACS) in MDA to fund cover crop activities on agricultural lands on which chicken manure has been applied as fertilizer. However, the Comptroller may distribute an amount necessary to administer the fee to an administrative cost account. The Comptroller may adopt regulations necessary to administer, collect, and enforce the fee.

The bill repeals the current distribution to MDA of 40% of bay restoration fees collected from users of septic systems and sewage holding tanks which is currently used to fund cover crop activities through MACS. As a result, 100% of those fees, rather than 60%, is deposited in the Septics Account of the Bay Restoration Fund (BRF) within MDE and used for the Septic System Upgrade Program.

Current Law/Background:

Bay Restoration – Generally

The Chesapeake Bay Total Maximum Daily Load (TMDL) established by the U.S. Environmental Protection Agency sets the maximum amount of pollution the bay can receive and identifies specific pollution reduction requirements. All reduction measures must be in place by 2025, with at least 60% of the actions established by 2017. Upgrading septic systems and planting cover crops are both pollution-reduction strategies identified in the State's Phase II Watershed Implementation Plan, the State's roadmap to achieving the nutrient pollution limits required under the TMDL.

Bay Restoration Fund

BRF was established in 2004 and is administered by the Water Quality Financing Administration within MDE. The main goal of the fund 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 and to support septic system upgrades and the planting of cover crops. The fund is supported by a bay

restoration fee on users of wastewater facilities, septic systems, and sewage holding tanks. The revenue collected from WWTP users is used to provide grants to upgrade the State's major WWTPs with ENR technology. Of the revenue collected from users of septic systems and sewage holding tanks, 60% is distributed to MDE's Septics Account for the upgrade of septic systems and costs of local government efforts to ensure compliance with septic system regulations and 40% is transferred to MACS within MDA to provide assistance to farmers for planting cover crops.

In fiscal 2014, revenue collected from users of septic systems and sewage holding tanks totaled approximately \$28 million, with 60% (\$16.8 million) distributed to MDE and 40% (\$11.2 million) distributed to MDA.

Cover Crops and MACS

The State is implementing a variety of agricultural best management practices (BMPs) to reduce pollution loads, including constructing animal waste structures, expanding stream protection, and updating farm soil conservation and water quality plans. However, the agricultural BMP that has arguably received the most policy attention and financial support is the winter cover crop program. Cover crops are cereal grains and winter annual brassicas (plants in the cabbage family) that are planted in the fall to take up nutrients that remain in the soil following the harvest of corn, soybeans, sorghum, tobacco, or vegetables. Cover crops grow through the winter and recycle unused plant nutrients, protect fields against wind and water erosion, and help improve the soil for the spring crop.

MACS, administered by MDA, provides cost-share funding for various types of agricultural BMPs, including cover crops. The cover crop program within MACS is funded with special funds from BRF and the Chesapeake and Atlantic Coastal Bays 2010 Trust Fund. The 2010 Trust Fund receives a portion of revenues from the motor fuel tax and the sales and use tax on short-term vehicle rentals and is used to fund nonpoint source pollution control projects. The Governor's proposed fiscal 2016 budget includes \$11.2 million from BRF and \$11.3 million from the 2010 Trust Fund for MDA's cover crop program.

Poultry Integrators

Poultry integrators are companies that contract with farmers (or "growers") to raise the companies' birds. The farmers own the chicken houses and equipment, but the companies provide the chicks, feed, bedding materials, propane gas for heating, health care for the chickens, and technical assistance. There are five poultry integrators on the Eastern Shore that contract with more than 700 farmers in Maryland to raise chickens for the poultry integrators.

State Fiscal Effect:

Maryland Department of Agriculture – Cover Crop Activities

Revenues

MDA special fund revenues for cover crop activities increase by approximately \$0.1 million in fiscal 2016 and by approximately \$3.8 million annually thereafter. This reflects the net annual increase resulting from an annual decrease of \$11.2 million in BRF revenues and an annual increase of \$15.0 million in chicken manure pollution fee revenues. For fiscal 2016, the estimate accounts for only 75% of the chicken manure pollution fee revenue due to the October 1, 2015 effective date of the fee. This estimate is based on:

- the \$11.2 million from BRF included in the Governor’s proposed fiscal 2016 budget for the cover crop program; and
- the \$0.05 fee applied to an approximate number of chicks provided by poultry integrators to farmers in Maryland each year of 300 million.

Exhibit 1 shows the MDA special fund revenue impact in the context of the overall revenue and expenditure impacts of the bill in fiscal 2016.

The bill authorizes the Comptroller to distribute an amount of the chicken manure pollution fee revenue necessary to administer the fee to an administrative cost account. However, the Comptroller’s Office is expected to handle administration of the fee with existing resources, allowing for the full amount of fee revenue collected to be transferred to MDA.

Expenditures

Under the bill, MDA special fund expenditures for cover crop activities are expected to *decrease* by \$4.9 million in comparison to the \$11.2 million from BRF included in the Governor’s proposed fiscal 2016 budget for the cover crop program. According to MDA, the restriction under the bill on the use of the chicken manure pollution fee revenues only for cover crop activities *on land upon which chicken manure has been applied as fertilizer* limits the funding to be used for cover crop planting to only 110,000 to 132,000 acres. Assuming an average payment of \$50 per acre for cover crop planting on 120,000 acres, \$6.0 million is paid out in cover crop grant funding under the bill. Assuming that the administrative costs of the cover crop program, which are currently covered by BRF fee revenue, are covered instead by the chicken manure pollution fee revenue, an additional \$300,000 is spent on administrative costs, resulting in \$6.3 million in total special fund expenditures for cover crop activities funded by the chicken manure pollution fee revenue in fiscal 2016.

Exhibit 1
Fiscal 2016 Cover Crop and Septic System Upgrade Funding
(\$ in Millions)

| | <u>Current Law</u> | <u>Under the Bill</u> | <u>Increase/ (Decrease)</u> |
|-----------------------------------|--------------------|-----------------------|---------------------------------|
| MDA – Cover Crops* | | | |
| BRF Revenues | \$11.2 | – | (\$11.2) |
| CMPF Revenues | – | \$11.3** | 11.3 |
| <i>Net Revenue Incr./ (Decr.)</i> | | | <i>0.1</i> |
| Expenditures | 11.2 | 6.3 | (4.9) |
| MDE – Septic Systems | | | |
| BRF Revenues | 16.8 | 28.0 | 11.2 |
| Expenditures | 16.8 | 28.0 | 11.2 |
| Total | | | |
| Revenues | \$28.0 | \$39.3 | \$11.3 |
| Expenditures | \$28.0 | \$34.3 | \$6.3 |

*The cover crop program also receives funds from the Chesapeake and Atlantic Coastal Bays 2010 Trust Fund (\$11.3 million in the Governor’s proposed fiscal 2016 budget), but that funding source is not affected by the bill and is not reflected in this exhibit.

**This reflects 75% of the annual revenue of \$15 million, due to the October 1, 2015 implementation date of the new fee.

BRF: Bay Restoration Fund
CMPF: chicken manure pollution fee

Source: Department of Legislative Services

Accumulation of Unused Funding

Because the bill requires the chicken manure pollution fee revenue to be used for a specific purpose (cover crop activities on agricultural lands upon which chicken manure has been applied as fertilizer), unused funding in a fiscal year is expected to carryover and be available in the following years. Since revenues are greater than expenditures, as described above, it appears that a significant fund balance accrues over time.

Maryland Department of the Environment – Septic System Upgrades

MDE special fund revenues and expenditures for the Septic System Upgrade Program increase by \$11.2 million as a result of 100% of bay restoration fees collected from users of septic systems and sewage holding tanks, rather than 60%, being deposited in the Septics Account of BRF and used for septic system upgrades and local regulation compliance. MDE is authorized to retain up to 8% of Septics Account revenues to cover administrative expenses and the remainder, at least \$10.3 million, is provided to local governments for regulation compliance and to administer grants for septic system upgrades.

Local Fiscal Effect: Local government revenues and expenditures increase correspondingly by at least \$10.3 million each year, reflecting additional revenues received from MDE and the spending of those revenues on regulation compliance and grants for septic system upgrades.

Small Business Effect:

Chicken Manure Pollution Fee

If the establishment of the chicken manure pollution fee causes chicken production to leave the State to any extent, small business farmers that raise chickens and other small businesses that provide products and services to the industry are negatively impacted.

Reduction in Cover Crop Funding

Because the bill is expected to *reduce* spending on cover crops, small businesses in input industries, such as seed suppliers and equipment contractors (which contract to plant and harvest the crops with the contractors' equipment) are negatively impacted. Farmers who would have utilized the cover crop funding in the absence of the bill are also negatively impacted due to the loss of the soil retention and soil health benefits of cover crops.

Increase in Septic System Upgrade Funding

Because the bill increases funding available for septic system upgrades, small businesses that install upgrades may benefit.

Additional Information

Prior Introductions: SB 725 of 2014 received a hearing in the Senate Education, Health, and Environmental Affairs Committee, but no further action was taken. Its cross file, HB 905, was referred to the House Environmental Matters Committee, but subsequently withdrawn.

Cross File: SB 533 (Senator Madaleno, *et al.*) - Education, Health, and Environmental Affairs.

Information Source(s): Maryland Department of Agriculture; Maryland Department of the Environment; Comptroller's Office; Harford, Montgomery, and Talbot counties; Baltimore City; Delmarva Poultry Industry, Inc.; Department of Legislative Services

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min/lgc

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