LEGISLATIVE SERVICES AGENCY
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FISCAL IMPACT STATEMENT

LS 7187 **NOTE PREPARED:** May 3, 2007
BILL NUMBER: HB 1722 **BILL AMENDED:** Apr 27, 2007

SUBJECT: Utility Matters.

FIRST AUTHOR: Rep. Stilwell **BILL STATUS:** Enrolled
FIRST SPONSOR: Sen. Hershman

FUNDS AFFECTED: X GENERAL **IMPACT:** State & Local
X DEDICATED
FEDERAL

Summary of Legislation: *Ethanol Production Tax Credit:* The bill provides that the total amount of Ethanol Production Tax Credits for taxpayers that produce at least 20,000,000 gallons of cellulosic ethanol in a year may not exceed $20,000,000 for all taxpayers for all taxable years, and the credits may be applied only to state tax liability attributable to business activity taking place at the Indiana facility at which the cellulosic ethanol was produced. The bill also provides that a taxpayer may not sell, assign, convey, or otherwise transfer an Ethanol Production Tax Credit.

Coal Gasification Technology Investment Tax Credit: The bill allows a taxpayer to assign part or all of a Coal Gasification Technology Investment Tax Credit to an electric utility that has entered a contract to purchase electricity or substitute natural gas from the taxpayer. It also provides that a facility that produces synthesis gas as a substitute for natural gas is eligible for a Coal Gasification Technology Investment Tax Credit.

Energy Savings Tax Credit: The bill creates a tax credit, beginning in taxable year 2009, for the purchase of energy star heating and cooling equipment manufactured in the United States.

Cost Recovery for Substitute Natural Gas: The bill requires the Utility Regulatory Commission (IURC) to allow a utility that purchases substitute natural gas (SNG) to recover any costs arising under the purchase contract through rate adjustments. The bill amends the definition of clean coal and energy projects to include a project using coal to produce substitute natural gas.

Substitute Natural Gas Property Interests: The bill defines an SNG property interest as a right, title, and interest that: (1) is held by an energy utility; (2) is created by a qualified order of the IURC; and (3) entitles

the energy utility to recover certain costs incurred in purchasing substitute natural gas under a qualified contract. The bill sets forth provisions governing: (1) the assignment of an SNG property interest; (2) the rights of assignees, financing entities, and SNG sellers; (3) the perfection of a lien and security interest in an SNG property interest; and (4) the obligations of an energy utility after the assignment of an SNG property interest.

Organic Biomass Definition: The bill specifically lists certain items included in the definition of organic waste biomass for purposes of the law concerning a utility's purchase of energy from alternative sources.

Water Utility Territorial Disputes: The bill provides that certain municipalities have jurisdiction over certain territorial disputes between water utilities.

Effective Date: Upon passage; July 1, 2007; January 1, 2008.

Explanation of State Expenditures: *IURC:* This bill will increase the administrative costs of the IURC by requiring amendment to current procedures for conducting cost recovery rate adjustment hearings. The amount of the increase in costs is indeterminable, but it is estimated that the IURC could implement these provisions through the use of existing staff and resources.

Background: The operating budgets of the IURC and OUCC are funded by regulated utilities operating in Indiana. The IURC determines the rate at which to bill the utilities based on the two agencies' budgets, less reversions, divided by the total amount of gross intra-state operating revenue received by the regulated utilities for the previous fiscal year. Based on this formula, utilities are currently billed approximately 0.15% of their gross intra-state operating revenues to fund the IURC and OUCC. In FY 2006, fees from the utilities and fines generated approximately $11.8 M.

Cost Recovery for Substitute Natural Gas: This bill allows facilities that generate substitute natural gas to apply to the IURC for a rate adjustment to recover costs. The bill also adds production facilities to the definition of eligible business in IC 8-1-8.8-6 and the definition of new generating facility under IC 8-1-8.8-8. The bill, by adding these facilities to these definitions, is allowing these facilities to seek rate adjustments for cost recovery and financial incentives from the IURC currently provided by statute to clean coal and energy projects, construction or repower of a new energy generating facility, and development of alternative and renewable energy resources.

By allowing these rate adjustments for cost recovery this bill will impact the state if it purchases utility service from a facility that produces substitute natural gas. The amount of the increase in costs is indeterminable, and could be offset by the possible increase in Utility Receipts Tax (URT) and Utility Services Use Tax collections (USUT) from the increase in receipts by these utilities increasing rates.

Background: The rate for both the URT and USUT is 1.4%. The URT is calculated on the gross receipts of all entities providing the retail sale of utility services in Indiana. The USUT is imposed on the retail consumption of utility services in Indiana.

Department of State Revenue (DOR): The DOR would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to incorporate the Energy Savings Tax Credit, the Ethanol Production Tax Credit, and the expansion of the Coal Gasification Technology Investment Tax Credit. The DOR's current level of resources should be sufficient to implement these changes.

Explanation of State Revenues: *Ethanol Production Tax Credit:* The bill provides for a separate tax credit for cellulosic ethanol production, provided the taxpayer produces at least 20 M gallons of cellulosic ethanol in a taxable year. The tax credit would be effective beginning in tax year 2008. The tax credit may be applied against the Adjusted Gross Income Tax liability, Insurance Premiums Tax liability, or Financial Institutions Tax liability. Under the credit, the Indiana Economic Development Corporation (IEDC) would be able to determine the maximum credit for a taxpayer, but the bill would limit the total credits awarded to $20 M for all taxpayers for all taxable years. The bill limits application of this tax credit to state tax liability attributable to business activity at the Indiana facility where the cellulosic ethanol is produced. The bill also specifies that the current $50 M aggregate limit on all tax credits for grain ethanol production and biodiesel production does not apply to the new tax credit for cellulosic ethanol production.

Background: Grain ethanol and cellulosic ethanol are the same product, but are produced utilizing different feedstocks and processes. Grain ethanol is produced from corn, wheat, or soybeans. Cellulosic ethanol can be produced from agricultural plant waste, plant wastes from industrial processes, and energy crops grown specifically for fuel production, such as switchgrass.

Coal Gasification Technology Investment Tax Credit: The bill makes the following two changes to this tax credit.

(1) The bill expands the tax credit to include investment in a facility that converts coal into synthesis gas which is then used as a substitute for natural gas. As the change is effective upon passage, the expansion of the tax credit would be effective beginning in tax year 2007. Current statute limits the tax credit to investment in a facility that converts coal to synthesis gas and then uses the synthesis gas to generate electric energy. The potential amount of tax credits that may be granted for coal gasification facilities for the purpose of producing a substitute for natural gas is indeterminable and will depend upon review and approval of creditable investment by the IEDC; and determinations by the IURC that the public convenience and necessity requires the installation of the facilities.

(2) The bill allows a taxpayer receiving the tax credit to assign part or all of the credit to a utility that has entered into a contract: (1) approved by the IURC; (2) providing for the purchase of electricity or substitute natural gas by the utility from the taxpayer under provisions of the bill; and (3) expressly allowing the assignment of the tax credits. The utility would be able to apply the assigned credits against the tax liability arising under the Adjusted Gross Income (AGI) Tax, Financial Institutions Tax, Insurance Premiums Tax, and Utility Receipts Tax. The bill requires the utility to take the credit in 20 annual installments. The bill also limits the annual amount that the utility may claim to the greater of: (1) 25% of the utility's state tax liability under the taxes listed above; or the utility's total Utility Receipts Tax liability for the taxable year.

Background: The coal gasification technology investment tax credit may be taken against a taxpayer's tax liability arising under the Adjusted Gross Income (AGI) Tax, Financial Institutions Tax, Insurance Premiums Tax, and Utility Receipts Tax. The tax credit is for qualified investment in an integrated coal gasification power plant which converts coal to synthesis gas and uses the synthesis gas to generate electric energy. The credit is equal to 10% of the first $500 M in qualified investment, and 5% of the qualified investment exceeding $500 M.

Energy Savings Tax Credit: The bill establishes a nonrefundable tax credit for expenditures on energy star heating and cooling equipment by individual and corporate taxpayers against the Adjusted Gross Income (AGI) Tax, Insurance Premiums Tax, and Financial Institutions Tax liability. The tax credit applies to expenditures by individuals and small business on energy star furnaces, water heaters, central air conditioning systems, room air conditioners, and programmable thermostats. The bill defines a "small business" as an independently owned and operated business with its principal office located in Indiana. To be a "small business" the business may not have more than 100 employees and its average annual gross receipts may not exceed $10.0 M, unless it's a manufacturing business in which case it only has to meet the employment requirement. The tax credit is equal to the lesser of 20% of the amount of expenditures on such equipment during the taxable year or $100. The bill limits to $1.0 M the aggregate amount of credits that may be allowed in a state fiscal year. Data on annual energy star purchases in Indiana, purchase prices, and average net tax liabilities suggests that the annual revenue loss will reach the $1.0 M annual limit. Since the credit is effective beginning in tax year 2009, the fiscal impact is expected to begin in FY 2010.

Cost Recovery for Substitute Natural Gas: By allowing rate adjustments for more facilities to recover costs this bill could increase URT and USUT collections. Any increase in collections will ultimately be determined by the increase in receipts for a utility that is permitted the IURC to adjust their rates for cost recover under the bill.

Explanation of Local Expenditures: *Cost Recovery for Substitute Natural Gas:* By allowing these rate adjustments for cost recovery this bill will impact local units of government which purchase utility service from a facility that produces substitute natural gas. The amount of the increase in costs is indeterminable.

Explanation of Local Revenues:

State Agencies Affected: Department of State Revenue; Utility Regulatory Commission; Indiana Economic Development Corporation;

Local Agencies Affected:

Information Sources: Bill McNary, D and R International, 301-588-9387. U.S. EPA and U.S. Department of Energy, www.energystar.gov.

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