

NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

ELECTRIC INDUSTRY COMPETITION COMMITTEE

Wednesday, December 1, 1999
Woodland East Room, Doublewood Inn
3333 13th Avenue South
Fargo, North Dakota

Representative Al Carlson, Chairman, called the meeting to order at 9:00 a.m.

Members present: Representatives Al Carlson, Robert Huether, Matthew M. Klein; Senators Randel Christmann, Pete Naaden, Larry J. Robinson

Others present: See Appendix A

It was moved by Senator Robinson, seconded by Senator Christmann, and carried on a voice vote that the minutes of the October 15, 1999, committee meeting be approved as distributed.

Chairman Carlson called on Mr. Richard Bulman, General Manager and Chief Operating Officer, MAPPCOR, St. Paul, Minnesota, to address the committee. A copy of the overheads used by Mr. Bulman in his presentation is attached as Appendix B. He said MAPPCOR is an association of utilities in the Upper Midwest, and Mid-Continent Area Power Pool (MAPP) is an association of utilities and other related organizations in the Upper Midwest. Following the New York City electrical blackout of 1965, he said, various industry interests believed it would be beneficial to develop industrywide reliability standards to ensure reliable electric service. He said this led to the North American Electricity Reliability Council, which is composed of 10 regional councils of which MAPP, or the Mid-Continent Area Power Pool, is one. He said each organization works to establish reliability standards within its region and with other regional entities to formulate reliability standards for North America.

Mr. Bulman said MAPP is composed of organizations in the region that participate in the industry including cooperatives, municipal power agencies, utilities, and public power districts. In 1996, he said, MAPP allowed independent power marketers and producers to join. Also, he said, governmental entities such as the Western Area Power Administration and Canadian crown corporations have always been members. He said there are 97 entities that participate in MAPP, including state regulatory bodies. He reviewed the structure and responsibilities of the financial committee, administrative oversight committee, executive committee, power and energy market committee, regional reliability committee, and regional transmission committee. He said the duty of the regional transmission committee is to provide for the

efficient provision of transmission service within and contiguous to the MAPP region on a consistent basis and to administer a regional tariff.

Concerning implementation of an independent system operator, Mr. Bulman said the Federal Energy Regulatory Commission has identified 11 principles for establishing this entity. He said governance should be structured in a fair and nondiscriminatory manner; there should be no financial interest in the economic performance of any power market participant; there should be open access to transmission systems pursuant to a single, unbundled, gridwide tariff to all eligible users; the independent system operator should have primary responsibility for short-term reliability; the independent system operator should have control over the operation of interconnected transmission facilities within its region; the independent system operator should identify and assume operational actions to relieve constraints; and the independent system operator should establish appropriate incentives for efficient management and administration. He said an independent system operator should establish pricing policies to promote the efficient use of investment in generation, transmission, and consumption; provide publicly available information on a timely basis by an electronic information network; develop mechanisms to coordinate with neighboring control areas; and establish an alternative dispute resolution process. He then reviewed the criteria for establishing a regional transmission organization. He said a regional transmission organization must be independent from market participants and must include a region of sufficient scope and configuration, have operational responsibility for all transmission facilities, and have exclusive authority for maintaining short-term reliability.

Concerning the regional transmission organization timeline, Mr. Bulman said conditional changes to the restated agreement to provide for the creation of a regional transmission organization were sent to members for a vote on October 8, 1999. He said December 7, 1999, is the due date for the membership to vote on establishing a regional transmission organization. Finally, he reviewed the provisions of the MAPP/Midwest Independent System Operator Memorandum of Understanding.

In response to a question from Representative Carlson, Mr. Bulman said implementation of an independent system operator would move management away from the various stakeholders to an independent board and give market participants who are not owners of transmission a higher level of comfort that they are receiving adequate access to transmission.

In response to a question from Representative Huether, Mr. Bulman said implementation of an independent system operator would not result in any change in ownership of transmission lines. In response to a further question from Representative Huether, Mr. Bulman said the independent system operator or regional transmission organization would be responsible for determining whether additional transmission facilities should be constructed.

In response to a question from Representative Carlson, Mr. Bulman said a regional transmission organization would probably be implemented by the Federal Energy Regulatory Commission and companies that are subject to the Federal Energy Regulatory Commission will probably join a regional transmission organization.

At the request of Chairman Carlson, committee counsel reviewed a memorandum entitled *Constitutional and Other Considerations Regarding Imposing a Megawatt Per Hour Tax on Municipal Power Systems* and a memorandum entitled *Constitutional Issues Concerning Implementation of a Megawatt Per Hour Tax and the Role of the State Board of Equalization*.

Chairman Carlson called on Mr. Harlan Fuglesten, Communications and Government Relations Director, North Dakota Association of Rural Electric Cooperatives, to address the committee. A copy of Mr. Fuglesten's written comments is attached as Appendix C. He reviewed the investor-owned utility tax proposal and compared that proposal to the Association of Rural Electric Cooperatives' utility taxation proposal. In summary, he said, the revised rural electric cooperative tax plan would leave in place the current coal conversion taxes and would be made applicable to all coal conversion plants of five megawatts or more. Concerning the transmission function, he said, the rural electric cooperative proposal would tax all transmission facilities on a line mile basis based on the rate of \$75 per line mile to \$900 per line mile. The distribution function, he said, would be taxed using a two-part formula. There would be a flat tax of 59 cents per megawatt hour and a tax of .95 percent of revenue collected on the retail sale of electricity, he said.

Chairman Carlson called on Mr. Dennis Boyd, Montana-Dakota Utilities Company, who said the utility taxation working group has had one meeting since the committee's last meeting at which the Association of Rural Electric Cooperatives' and investor-owned utility's tax proposals were reviewed. Mr. Boyd said the investor-owned utilities have also met to

discuss the two proposals. He said the investor-owned utilities believe there are similarities in the two proposals and areas of agreement. He said the investor-owned utility tax proposal is an effort to simplify and bring equity to the taxation of the electric utility industry whereby all competitors pay exactly the same taxes at exactly the same rate.

Chairman Carlson called on Mr. Bruce J. Kopp, Northern States Power Company, who said if the tax proposals are to be revenue neutral and the transmission component is less than that proposed in the investor-owned utility proposal, then taxes must be shifted to the distribution component which are paid by North Dakota citizens rather than by nonresidents. Mr. Kopp said the transmission component contained in the investor-owned utility tax proposal is more fair to all individuals affected by the tax.

Concerning the distribution component, Mr. Kopp said, the revisions made by the Association of Rural Electric Cooperatives are minimal. He said this tax shifts the electric utility tax burden from out-of-state electricity purchasers to North Dakota residents and the percentage of revenue component may lead to revenue erosion for the state.

In summary, Mr. Kopp said, the taxation issue may be reduced to three points. Number one, he said, what taxes does the committee wish to include in the proposals? He said the investor-owned utilities believe that all taxes paid by electricity providers should be included in the final tax proposal. Second, he said, how much should be allocated to the transmission component and how much to the distribution component? And finally, he said, which methodology is best to develop a distribution tax component? He said the investor-owned utility proposal benefits the state and all consumers in the state.

In response to a question from Senator Robinson, Mr. Kopp said the investor-owned utility tax proposal calling for elimination of the corporate income tax paid by electric utilities is revenue neutral, and thus other corporate taxpayers would not be able to argue that they are entitled to a corporate tax reduction because granting a corporate income tax reduction to another entity would result in revenue loss to the state. He said if the proposal advocated by the Association of Rural Electric Cooperatives is adopted, the state is essentially saying it wants to tax North Dakota residents because it does not want to increase taxes for nonresidents.

In response to a question from Representative Huether, Mr. Kopp said if the investor-owned utility tax proposal is adopted, it would not make lignite uncompetitive with other energy sources, and he noted that transmission facilities in North Dakota are undervalued and the investor-owned utility tax proposal seeks to rectify this situation.

In response to a question from Representative Huether, Mr. Kopp said in states that have restructured their electric utility industry, rates have either

decreased or stayed the same. Thus, he said, if the state were to adopt a percentage of revenue tax and rates decreased, the state would experience revenue erosion.

Chairman Carlson called on Ms. Marcy Douglas, Auditor, City of Northwood, who addressed the committee. A copy of her written comments is attached as Appendix D. She reviewed the impact of the investor-owned utility's tax proposal on municipal power systems and the effect of municipal distribution systems on the property tax revenue for school districts. She said the municipal power systems welcome the opportunity to reconvene the electric industry utility taxation task force to discuss the two tax proposals before the committee.

In response to a question from Senator Naaden, Ms. Douglas said cities with municipal power systems are reaping the natural benefit of the bargain they struck many years ago to obtain preference power and establish municipal power systems. As a result of this bargain, property taxes may be lower and cities with municipal power systems may be able to provide services that other cities cannot, she said.

In response to Ms. Douglas's comments, Senator Naaden said cities with municipal power systems receive favorable treatment in the school funding formula because of their municipal power systems.

In response to a question from Representative Carlson, Ms. Douglas said implementation of the original Association of Rural Electric Cooperatives' electric utility taxation proposal would result in a revenue loss of \$17,393 to the city of Northwood and the investor-owned utility proposal would result in a revenue loss of \$19,479.

In response to Ms. Douglas's comments, Representative Carlson said neither proposal submitted to the committee would restrict a municipal power utility from transferring revenue to the general fund of a city and that is not the intent of the committee.

In response to a question from Representative Carlson, Ms. Douglas said the city of Northwood has adopted an ordinance that would impose a franchise fee for electricity providers.

Chairman Carlson called on Ms. Marcy Dickerson, Utility Tax Appraiser, Tax Department, to address the committee. A copy of her written testimony is attached as Appendix E. She reviewed the impact of the restructuring of the contract between Central Power Electric Cooperative and Upper Missouri Generation and Transmission Electric Cooperative and Basin Electric Power Cooperative and reviewed the two tax proposals submitted to the committee.

In response to a question from Representative Carlson, Ms. Dickerson said there are a number of different methods that could be used to distribute revenue generated by a distribution tax on electricity. One method, she said, would be similar to that used to distribute the telecommunications tax revenue in which the amount of money received by each political

subdivision in a base year from property taxes and the old telecommunications tax is used to establish a new base level of revenue. The advantage to this system, she said, is that each political subdivision knows the amount of revenue it will receive in any given year. The disadvantage to this system, she said, is that it does not provide any revenue growth for political subdivisions.

In response to a question from Representative Carlson, Ms. Dickerson said she would provide information on alternatives that the committee could review to distribute an electricity distribution tax.

In response to a question from Representative Carlson, Mr. Fuglesten said the contract provisions between Central Power and Basin Electric will result in approximately \$800,000 less revenue to the state per year.

Chairman Carlson called on Mr. Mark Johnson, Executive Director, North Dakota Association of Counties, who said the association does not like the "pot" effect in that having the state collect revenue and then reallocate it to political subdivisions through a formula may lead to an increase or decrease in revenue for some political subdivisions. He said the association would like to retain some sort of tax based on property. If one of the objectives of a revised electric utility tax is simplicity, he said, the committee would not be meeting this goal if the property tax is eliminated, and the committee would also not meet its stated goal of not harming political subdivisions. He said the association supports the concept of a direct appropriation so political subdivisions would participate in any growth or decrease in revenue. He said the committee should review different distribution alternatives.

Chairman Carlson called on Mr. Jerry Hjelmstad, Assistant Director, North Dakota League of Cities, who said that any electric utility taxation revision should provide the same amount of revenue to the state's cities and political subdivisions as do the current gross receipts and property taxes.

Chairman Carlson called on Mr. Fuglesten, who said he disagreed with Mr. Kopp's assertion that the corporate income tax currently paid by the state's investor-owned utilities is not shifted to the rural electric cooperatives under the investor-owned utility tax proposal. He said the investor-owned utility tax proposal increases transmission and distribution taxes by \$2.5 million with an increase of \$3 million on transmission and a decrease of \$500,000 on distribution. The net effect of the investor-owned utility taxation proposal, he said, is to reduce investor-owned utility taxes by \$1 million and to increase taxes for rural electric cooperatives by over \$1 million. He said the investor-owned utility tax proposal shifts the corporate income tax from the state's investor-owned utilities to the rural electric cooperatives. Concerning transmission, he said, the rural electric cooperatives have made a significant compromise and the

investor-owned utilities have not put forward a compromise or alternative proposal on transmission. He said the transmission component contained in the investor-owned utility proposal would be devastating for the state's rural electric cooperatives. Concerning the issue of revenue erosion, he said, the opposite could be true in that if electric utility rates increase in a deregulated market, the state will realize increased revenue. He said the two-part distribution formula contained in the rural electric cooperative proposal reflects that 50 percent of the distribution tax would be collected on the basis of the actual sale price of electricity, which reflects the difference in cost to the users of electricity. Finally, he said, the electricity taxation proposal submitted by the rural electric cooperatives is a package and is intended to work as a package, and the association does not view it as a "pick or choose" plan in which the committee could adopt a portion of the proposal but not the entire package.

In response to a question from Senator Robinson, Mr. Fuglesten said marginal progress could be made to resolve the differences between the rural electric cooperative and the investor-owned utility tax proposals. However, he said, if some understanding is not reached on the income tax credit issue, the differences may not be resolvable.

Chairman Carlson called on Mr. Boyd, who said it appears that there is substantial agreement between

the rural electric cooperatives and the investor-owned utilities on the generation component. Mr. Boyd said the state's investor-owned utilities are willing to work with the rural electric cooperatives on resolving the differences in the transmission and distribution components of the two proposals. One alternative to resolve the corporate income tax issue, he said, would be to enact a tax, similar to one enacted by the state of Alaska, to impose a cooperative tax in lieu of a corporate income tax on the state's rural electric cooperatives. He said this would essentially nullify the corporate income tax issue and treat the cooperatives the same as the state's investor-owned utilities.

Chairman Carlson requested that the state's investor-owned utilities and the Association of Rural Electric Cooperatives continue to work to resolve their differences and include any other interested parties in their discussions.

No further business appearing, Chairman Carlson adjourned the meeting at 3:30 p.m.

Jeffrey N. Nelson
Committee Counsel

ATTACH:5