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LOCAL FINANCE NOTICE

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ENERGY DEREGULATION AND UTILITY TAXATION: ITS IMPACT ON MUNICIPALITIES

The deregulation of energy and the advent of competition in what has traditionally been a monopoly industry in New Jersey has necessitated the reform of energy and utility taxation. Recently enacted laws have changed the way energy and utility companies are taxed. This Local Finance Notice reviews the recent changes.

Prior to the law change, approximately 13 percent was levied in excise taxes on energy and telecommunications companies (i.e., PSE&G, GPU Energy, New Jersey Natural Gas, Bell Atlantic) in lieu of allowing municipalities to levy property taxes on energy and telecommunications property and installations. These companies passed these taxes along to ratepayers on their utility bills. Funds were generally allocated to municipalities based on the value of utility equipment and facilities located in each municipality. Governor Whitman recently signed P.L. 1997, c. 162 to eliminate the Gross Receipts and Franchise Tax (GR&FT) on electric, natural gas, and telecommunications utilities, and P.L. 1997, c. 167 to replace the current method of distributing funds received from the Gross Receipts and Franchise Tax.

As of July 1, 1997, Chapter 167 created the "Energy Tax Receipts Property Tax Relief Fund" as a special dedicated fund to replace the Gross Receipts and Franchise Tax. Revenue for the Fund will be raised by applying:

- the Sales and Use Tax to energy or utility services;
- the Corporation Business Tax to electric and natural gas utilities, municipal or otherwise, that were subject to the Gross Receipts and Franchise Tax prior to January 1, 1998;
- the Corporation Business Tax to telecommunications utilities that were subject to the Gross Receipts and Franchise Tax as of April 1, 1997;
- the Gross Receipts and Franchise Tax to privately owned sewerage and water corporations as before.

In addition, Chapter 162 created the "Transitional Energy Facility Assessment Act" as a new, temporary revenue source assessed on natural gas and electric companies that were subject to the GR&FT prior to January 1, 1998.

Finally, the law requires the Legislature to appropriate any additional sums from the General Fund as will be necessary to provide mandated amounts to the Energy Tax Receipts Property Tax Relief Fund. That requires the State to deposit $740 million in this fund in FY 1998, $745 million in FY 1999, $750 million in FY 2000 and FY 2001, and $755 million in FY 2002 and each fiscal year thereafter. Any portion of the Energy Tax Receipts Property Tax Relief Fund left over will be distributed in the same proportion as the Energy Tax Receipts. These amounts have been calculated and provided to municipal Chief Financial Officers (Local Finance Notice CFO 97-11 and CFO 97-12 for SFY municipalities). Given the appropriation schedule, noted above, this provides annual increases in Energy Tax Receipts for the next five years.

With elimination of the Energy Unit Tax, the Sales and Use Tax will be applied to most retail sales of electricity. For most residents in municipalities with municipal electric utilities, life will go on the same as it always has (no extra taxes), with some special rules and considerations if their electric utilities spread into new service areas. These municipalities should carefully review the law to determine its effect on them.

The Energy Tax Receipts Program is allocated to ensure that municipalities will receive at least the same amount of money they received from the Gross Receipts and Franchise Tax. Each year municipalities will receive a sum at least equal to the largest annual amount received from:

- the $685 million distributed from the Gross Receipts and Franchise Tax in calendar year 1994, 1995, or 1996, plus;
- the taxes collected in replacement of the supplemental Gross Receipts and Franchise Tax for FY 1998.

The FY 1998 distribution of $35 million in supplemental Gross Receipts money will be paid on or before June 30, 1998. The ETR payment schedule uses the same payment schedule as other State aid, 35 percent on July 15, 10 percent on August 1, 30 percent on September 1, 15 percent on October 1, 5 percent on November 1, and 5 percent on December 1.

The new Energy Tax Receipts Property Tax Relief Fund is designed to see that New Jersey's municipalities continue to rely on this source of State aid as they have counted on it in the past. If you have any questions concerning the change in energy and utility taxation, and its effect on municipalities, please contact the Division at (609) 292-4656.

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