COMMITTEE ON WAYS AND MEANS
Senator Jill N. Tokuda, Chair
Senator Ronald D. Kouchi, Vice Chair

HEARING DATE: Monday, April 6, 2015
TIME: 1:30 p.m.

House Bill No. 1471 HD2 SD1 Relating to the Funding of Government Programs

Testimony of Jeff Walsh
President and General Manager of AES Hawaii, Inc.

Background

Chair Tokuda, and members of the Committee on Ways and Means, I am Jeff Walsh, President of AES Hawaii, Inc. ("AES Hawaii"), an independent power producer on Oahu producing electricity for Hawaiian Electric Company, Inc. ("HECO") using coal, among other recycled fuels such as tire-derived fuel, spent oil, and spent activated carbon to generate about 20% of island load at any time. In addition, AES Hawaii is currently permitted and capable of using up to 20% of renewable biomass to generate electricity, and is currently investigating the use of other recycled and renewable fuel to generate electricity.

AES Hawaii has provided safe, reliable and affordable power for the past 22 plus years. AES Hawaii has a Power Purchase Agreement to provide power to HECO, and is the lowest cost provider of energy to HECO on Oahu and in the State of Hawaii.

The AES Hawaii plant utilizes state of the art clean coal technology to effectively comply with all current federal and state environmental standards. Current emissions controls devices are as follows:

- Particulate removed by a fabric filter bag-houses which is the Best Available Control Technology or BACT.
- NOX control using "in-combustion" Selective Non Catalytic Reduction by injection of anhydrous ammonia.
- SOX control using in bed injection of locally mined limestone.

The AES Hawaii facility serves a critical service now and shall continue in the future to serve the citizens of Oahu. The plant provides by far the lowest cost energy on the island of Oahu under a long term contract with HECO. The energy pricing from this plant has provided stable and predictable energy pricing as compared to the highly variable costs of generating electricity with fuel oil.

AES Hawaii is Oahu's most reliable power plant from plant inception in 1992 to present with an availability factor of approximately 97%. With wind typically operating at 40-60% capacity factors and solar at 16-20% capacity factors, the stability of AES Hawaii complements and facilitates Hawaii's goal of increasing renewable energy.

AES Hawaii, the single largest generator connected to the HECO system, also provides firm capacity to the electric grid and provides dispatchable power which is used to control frequency and voltage on the island grid. This plays a critical role in maintaining grid stability.

Comments

AES Hawaii supports the bill as amended as HB 1471 HD2 SD1, which was previously amended to revise Section 2 of the bill (which amends HRS § 243-3.5) as previously requested by AES Hawaii. Accordingly, AES Hawaii has no further objections and supports this version of the bill.

AES Hawaii takes no position on PROPOSED HB1471 HD2 SD2.

Thank you for the opportunity to present this testimony.

Testimony before the
Senate Committee on Ways & Means

By Todd Kanja
Manager, LNG Enterprise Solutions
Hawaiian Electric Company, Inc.

Monday, April 6, 2015
1:30 pm, Conference Room 211

House Bill 1471, SD1 - Relating to the Funding of Government Programs

Chair Tokuda, Vice Chair Kouchi, and Members of the Committee:

My name is Todd Kanja and I am testifying on behalf of Hawaiian Electric Company, Inc. and its subsidiaries, Hawaiʻi Electric Light Company, Inc. and Maui Electric Company, Ltd.

HB 1471 SD1 proposes to amend Hawaiʻi Revised Statutes ("HRS") Chapter 243 to establish a new tax of $0.19 on each one million British thermal unit ("Btu") of "fossil fuel, other than petroleum product sold by a distributor to any retail dealer or end user, other than a refiner, of fossil fuel". HB 1471 also adds definitions for the terms "barrel" and "fossil fuel". Finally, HB 1471 excludes from the fossil fuel tax coal that is used to fulfill a signed power purchase agreement between an independent power producer and an electric utility that is in effect as of June 30, 2015. <u>While we appreciate and support the intent of this bill and are not opposed to broadening the barrel tax to include other forms of fossil fuels, we are opposed to the bill as it is currently written and therefore request that the bill be amended. Our proposed revisions to HB 1471, SD1 are consistent with the revisions we proposed for SB 358, which the ENE/AGL Committees incorporated into SB 358, SD1. We prefer SB 358, SD1. In the alternative, with these revisions, we would be able to support this bill.</u>

First, the new proposed subsection, HRS § 243-3.5(b), does not tax "fossil fuels" in a manner that is consistent with the existing tax on "petroleum products". That is, "petroleum products" are taxed on a volumetric basis at a flat rate of $1.05 per barrel ("Bbl"). This bill, however, proposes to tax "fossil fuels" (i.e., natural gas, coal, etc) on an energy basis (i.e., million Btu ("MBtu")) at a rate of $0.19/MBtu. This rate would be equivalent to the $1.05/Bbl if the heat content for the fuel is 5.5 MBtu/Bbl. The majority of the fuel currently consumed by Hawaiian Electric, however, is low sulfur fuel oil ("LSFO"), which has a heat content of approximately 6.2 MBtu/Bbl. Hawaiian Electric also consumes smaller volumes of diesel, which has a heat content of approximately 5.86 MBtu/Bbl. Accordingly, as shown in the table that follows, this bill would create a tax advantage in favor of LSFO against other "fossil fuels" like coal and natural gas.

	Petroleum Total	Import Total*	LSFO**	Diesel**	Coal**	Natural Gas**

	Products*					
Tax, $/UM	1.05	1.05	1.05	1.05	3.800	0.198
MBtu/UM	5.497	5.899	6.2	5.86	20	1.04
$/MBtu	0.191	0.178	0.169	0.179	0.190	0.190
% Difference	0.0%	-6.8%	-11.3%	-6.2%	-0.5%	-0.6%

UM = Unit Measure = Bbl for Oil = Short Ton for Coal = 1,000 SCF for Natural Gas
* MBtu/UM EIA Monthly Energy Review, Table A.2, 2014
** MBtu/UM Hawaiian Electric Company Estimate

Like oil, fossil fuels like coal and natural gas are typically measured on a volumetric /mass basis (e.g., tons of coal, standard cubic feet ("scf") of natural gas, tonnes of liquefied natural gas). Accordingly, to simplify the calculation of this tax, we would propose to have the tax applied on a volumetric /mass basis for "fossil fuels" that are consumed for power generation. We also request that "fossil fuels" like coal and natural gas be subject to the tax at a rate equivalent to that of LSFO in order to avoid giving a tax advantage to one fuel over another. That way, in the event a fuel is displaced by another (e.g., LSFO displaced by natural gas), the net barrel tax on the fuel would not change.

We propose the tax rates of $0.175 per 1,000 standard cubic feet of natural gas, and $3.40 per short ton of coal.

	Petroleum Total Products*	Import Total*	LSFO**	Diesel**	Coal**	Natural Gas**
Tax, $/UM	1.05	1.05	1.05	1.05	3.400	0.175
MBtu/UM	5.497	5.899	6.2	5.86	20	1.04
$/MBtu	0.191	0.178	0.169	0.179	0.170	0.168
% Difference	0.0%	-6.8%	-11.3%	-6.2%	-11.0%	-11.9%

UM = Unit Measure = Bbl for Oil = Short Ton for Coal = 1,000 SCF for natural gas
* MBtu/UM = EIA Monthly Energy Review, Table A.2, 2014
**MBtu/UM HECO Estimate

Second, we note that HB 1471 does not propose to change the definition of "distributor" in HRS §243-1. HRS §243-1 defines "distributor" in terms of a "person" handling "liquid fuel", as that term is also defined in HRS §243-1. If the definition of "distributor" is not amended, it would be unclear who is responsible for paying the tax in the newly proposed addition to HRS §243-3.5. Hawaiian Electric, therefore, suggests amending the definition of "distributor" in HRS §243-1 to add the language "or fossil fuel" everywhere the term "liquid fuel" appears.

Third, we propose that the language of this bill be revised, beginning on page 3, line 6, to read: "In addition to subsection (a), the tax shall also be imposed on each **short ton of coal and each 1,000 standard cubic feet of natural gas** sold by a distributor to any retail dealer or end user of fossil fuel. The tax shall be **$3.40 for each short ton of coal, $0.175 for each 1,000 standard cubic feet of natural gas,**

and $0.19 on each one million British thermal units for **all other fossil fuels** sold by a distributor to any retail dealer or end user of fuel; provided that of the tax collected pursuant to this subsection. . ."

Fourth, for clarity, we suggest amending the first clause in each of sections (b)(1), (b)(2), and (b)(3) to read: "____ per cent of the tax on **the total tax collected from fossil fuels** shall be deposited into…".

Fifth, we propose to revise the exemption set forth in the proposed subsection (c) of the bill. This section exempts "coal used to fulfill a signed power purchase agreement between an independent power producer and an electric utility that is in effect as of June 30, 2015." Since coal is not presently subject to any tax, this exemption would benefit our customers since no new tax would be passed through to them as a result of costs associated with existing power purchase agreements ("PPAs") that Hawaiian Electric has with independent power producers ("IPPs"). However, to ensure that all fossil fuels are eventually subject to the same tax liabilities, we would ask that the proposed language make clear that the exemption only applies to existing PPAs in the form that is effective as of June 30, 2015. Any extension or amendment to the existing PPAs should not be subject to this exemption. To address this, we would propose to amend the language of the bill, beginning on page 4, line 9, to read as follows: "(c) The tax imposed under subsection (b) shall not apply to coal used to fulfill a signed power purchase agreement between an independent power producer and an electric utility **in the form** that is in effect as of June 30, 2015. **The tax shall be imposed on any extensions or amendments to the purchase power agreement.**"

Sixth, to ensure there are no coordination or timing issues with gaining PUC approval for recovering the tax, the bill should enable the electric utility to recover the cost of the tax imposed under subsection (b) through an appropriate surcharge to its customers without further approval of the public utilities commission. We proposed to amend the language of the bill, beginning on page 4, line 10 to read as follows: "In which case, the electric utility may recover the cost of the tax through an appropriate surcharge to the end user **without further approval** by the public utilities commission."

Finally, in order to fairly administer this tax, Hawaiian Electric proposes to have HB 1471 SD2 make clear that any tax imposed on a unit of fuel under Chapter 243 only be charged once, and not on each person in the chain of custody.

L E G I S L A T I V E   T A X   B I L L   S E R V I C E

TAX FOUNDATION OF HAWAII

126 Queen Street, Suite 304 Honolulu, Hawaii 96813 Tel. 536-4587

SUBJECT: FUEL, Broaden and reallocate environmental response, energy, and food security tax

BILL NUMBER: HB 1471, SD-1

INTRODUCED BY: Senate Committees on Energy and Environment and Commerce and Consumer Protection

EXECUTIVE SUMMARY: Initially, the 5 cents per barrel environmental response tax was established to address oil spills in state waters. It was temporarily increased to $1.05, much of which was earmarked to numerous special funds, and was scheduled to sunset on 6/30/30. This measure subjects gaseous and non petroleum based fossil fuels to the tax, which is a tax increase of about 25%.

The tax has taken on a life of its own and lacks transparency, and the special funds it feeds do not come under close scrutiny by either lawmakers or the public. The barrel tax should be repealed and all programs funded out of the environmental response tax should be funded through the general fund.

In addition, lawmakers should consider that this tax is highly regressive, in that it has a disproportionate impact upon those struggling to get by.

BRIEF SUMMARY: Amends HRS section 243-3.5(a) to provide that the environmental response tax shall be imposed on each unit of fossil fuel, other than petroleum products, at the rate of $0.19 on each one million British thermal units (BTUs) of fossil fuel; provided that: (1)___% of the tax collected under this section shall be deposited into the energy security special fund; (2)___% of the tax shall be deposited into the energy systems development special fund; and (3)___% of the tax shall be deposited into the agricultural development and food security special fund. The tax shall not apply to coal used to fulfill a signed power purchase agreement between an independent power producer and an electric utility that is in effect as of June 30, 2015. Allows an independent power producer to pass the tax on to an electric utility, who, in turn, may recover the cost of the tax through a surcharge subject to the approval of the public utilities commission. Allows a gas utility to recover the cost of the tax as part of its fuel adjustment charge.

Defines "fossil fuel" as a hydrocarbon deposit, such as coal, natural gas, or liquefied natural gas, derived from the accumulated remains of ancient plants or animals and used for fuel; provided that the term specifically does not include petroleum products. (Petroleum products are already subject to this tax and will continue to be subject to the tax.)

EFFECTIVE DATE: July 1, 2015

STAFF COMMENTS: The legislature by Act 300, SLH 1993, enacted an environmental response tax of 5 cents per barrel on petroleum products sold by a distributor to any retail dealer or end user. The collections of the tax were deposited into the environmental response revolving fund until such time the balance in the fund reached $7 million at which time the imposition of tax was suspended until the balance in the fund declined.

The legislature by Act 73, SLH 2010, increased the amount of the tax to $1.05 per barrel and provided that 5 cents of the tax shall be deposited into a newly established environmental response revolving fund; 15 cents shall be deposited into a newly established energy security special fund, 10 cents shall be deposited into a newly established energy systems development special fund; 15 cents shall be deposited into the newly established agricultural development and food security special fund; and the residual of 60 cents shall be deposited into the general fund between 7/1/10 and 6/30/15. Act 107, SLH 2014, extended the sunset date of the $1.05 environmental response, energy, and food security tax from 6/30/15 to 6/30/30. This measure would extend the environmental response tax to include gaseous and non petroleum fuels.

The environmental response tax was initially adopted for the purpose of setting up a reserve should an oil spill occur on the ocean waters that would affect Hawaii's shoreline. The nexus was between the oil importers and the possibility that a spill might occur as the oil product was being imported into the state. Now that the fund has become a cash cow, lawmakers have placed other responsibilities on the fund, including environmental protection, food security, and natural resource protection programs, energy conservation and alternative energy development, air quality, global warming, clean water, polluted runoff, solid and hazardous waste, drinking water, and underground storage tanks, including support for the underground storage tank program of the department of health.

The basic problem with the barrel tax is that it lacks transparency, and because the funds are earmarked they do not come under close scrutiny by either lawmakers or the public. Rather than perpetuating the problems of the barrel tax, it should be repealed and all programs that are funded out of the environmental response fund should be funded through the general fund. At least program managers would then have to justify their need for these funds. If general funds are insufficient to underwrite all the essential programs and programs such as those funded through the barrel tax, then lawmakers need to justify any increase in taxes which underwrite the general fund or lawmakers will be forced to set priorities for those precious general funds. Currently, lawmakers are able to side step that difficult task by creating these hidden taxes and earmarked funds like the barrel tax. By continuing to special fund these programs, it makes a statement that such programs are not a high priority for state government. This sort of proliferation of public programs needs to be checked as it appears to be growing out of hand and at the expense of the taxpayer.

To understand the magnitude of the increase being considered, consider that statistics from the U.S. Energy Information Administration (www.EIA.gov) tell us that Hawaii consumed 42.4 million barrels of oil in energy production in 2012. Multiply that by $1.05 and we are talking about $44.5 million in barrel tax. The same agency tells us that our total energy consumption in that same year was 280 trillion BTUs. This bill would impose the barrel tax on all fossil fuels at the rate of 19 cents per million BTUs consumed, meaning that if the bill passes we are looking at a total tax of up to $53.2 million, an increase of about 25%.

In these times, power is a necessity for almost all families and businesses. A 2012 study by the American Coalition for Clean Coal Electricity (http://www.americaspower.org/sites/default/files/Energy_Cost_-Impacts_2012_FINAL.pdf) tried to calculate how much in after-tax income goes to energy costs, including the electric bill and the cost of gas to drive the family car. For those with pretax income of less than $10,000, the study concluded that over 75% of after-tax income went toward energy costs in 2012. For those making $10,000 to $30,000, the percentage dropped to 24%; it went to 17% for those making $30,000 to $50,000; and it was 9% for those making $50,000 or more. These, of course, were national averages. Hawaii households use far less power than those in other states because of our climate; in 2012 we had the fourth lowest per capita energy use in the nation. But on the other hand, our electricity prices were the highest in the nation. When considered together, these cost estimates can't be too far off as they apply to people in Hawaii. So: if we increase tax on power production, we know the tax increases will be passed on to the ratepayers, and guess who gets hit the hardest? If you, as a lawmaker, don't want to overtax the poor, jacking up the barrel tax absolutely is not going to get us there.

Digested 4/4/15