
Public Hearing

before

SENATE BUDGET AND APPROPRIATIONS COMMITTEE

SENATE BILL No. 31

(“Revises taxation of gas, electric and telecommunications public utilities and sales of electricity, natural gas and energy transportation service under transitions to competitive markets”)

LOCATION: Committee Room 4
State House Annex
Trenton, New Jersey

DATE: May 21, 1997
1:30 p.m.

MEMBERS OF COMMITTEE PRESENT:

Senator Robert E. Littell, Chairman
Senator Peter A. Inverso, Vice-Chairman
Senator John H. Ewing
Senator Joseph M. Kyrillos Jr.
Senator Dick LaRossa

ALSO PRESENT:

Aggie Szilagyi
Office of Legislative Services
Committee Aide

David Rousseau
Assembly Democratic
Committee Aide



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SENATOR ROBERT E. LITTELL (Chairman): Good afternoon, everybody. Please take a seat. Where are the Democrats? Aren't they a part of this Committee?

We have to have a little decorum. We have the President of the Senate here today. We have the Treasurer-Designate, and we've got our BPU Commissioner and President of BPU, Herb Tate, here with us.

This is a meeting of the Senate Budget and Appropriations Committee. We're here today to take testimony only and ask questions about Senate Bill No. 30 -- No. 31, sorry. We've got them both on the list.

Senate Bill No. 31, the elimination of the gross receipt and franchise tax, a sales and use tax imposed on most gas and electric purchases, and lots of other good things.

Senator DiFrancesco.

SENATE PRESIDENT DONALD T. DiFRANCESCO:

Well, we hope there are a lot of other good things, and I want to thank the Committee for meeting today. I know it's not a regular day, but I think this legislation deserves special recognition and special attention so that all of those people involved and entities involved -- organizations -- can have the benefit of not only hearing testimony, but giving testimony.

Senate Bill No. 31, of which I am a sponsor along with Senator Inverso -- just in case you have questions, he can answer them (laughter) -- would restructure the State's energy tax codes. And the compelling reason why we should move forward with this legislation is mainly just plain and simple competition.

Our energy rates, as everyone knows, are among the highest in the nation. In fact, our rates are among the top three in the country. We've all talked about, heard about, even some have been critical of our reductions in the income tax, the corporate sales tax, all designed -- at least from my personal standpoint -- to improve the climate for business and industry. But regardless of that, our energy taxes have continued to be out of line with our competing states. Lower rates, more competitive rates, are essential if we really are to remain open for business.

The pending deregulation of the electric industry, which will forever change the scope and the nature of energy production and supply, gives both the opportunity and the impetus to undertake a much-needed review and reform of our energy taxes. Many other large industrial states have already taken steps to pave the way for deregulation, and with this legislation, New Jersey can take its first step toward leveraging the rate reductions expected in a deregulated energy market.

In fact, if this legislation is enacted, all utility consumers, both business and residential, can expect to see energy tax rates decrease as much as 45 percent in the next five years.

As I said earlier, this legislation is intended to improve our competitive position nationwide. It's also designed to develop a more competitive marketplace within our own State. For years, significant disparities have existed in the way the State taxes utility and nonutility entities. For example, electric utilities collect gross receipts and franchise taxes from all retail customers, but cogenerators do not. Nonutility generators pay

corporation business taxes and make in-lieu-of-property tax payments to host communities. Utilities do not.

Senate Bill No. 31 would not only eliminate these different tax treatments for energy providers, it would also create a reliable replacement for dwindling GRFT revenues. Increased access to untaxed nonutility sources has significantly reduced the tax that represents the second largest source of municipal budget revenue in New Jersey. The restructuring called for in this legislation replaces the GRFT tax with an across-the-board application of the corporate business tax, the imposition of the 6 percent sales tax on retail electric and natural gas sales, and the implementation of a transitional energy facilities assessment that will be phased out over a five-year period. This new tax system will provide a more predictable, manageable stream of revenue, one that this Legislature is guaranteeing to all municipalities through a related companion bill sponsored by Senator Inverso, known as the Energy Tax Receipt Property Tax Relief Act.

As a nation and as a State, we're at a crossroad. After decades as a regulated monopoly, the electric industry will be deregulated, and the ways in which electric energy is bought, sold, distributed, supplied, and taxed will be dramatically altered. Now, we can stand by and let other states like California or Massachusetts set the pace for lower, more competitive energy rates, or we can take charge of the inevitable changes expected under deregulation and put into place a new tax structure that will yield greater competition and, ultimately, lower energy rates for consumers.

So I ask all of you, at the appropriate time, to vote yes in support of Senate Bill No. 31 and in support, really, of a more equitable, affordable, electric marketplace.

That's all I have to say. I'll be happy to respond to questions. Both the President of the Board of Public Utilities is here, as well as the Treasurer to help in that regard. I really -- other than to admire this Committee room that you caused to be decorated for yourself, Bob, (laughter) -- I really have nothing else to say.

SENATOR LITTELL: Well, you shouldn't have said that. (laughter) I did it for you.

SENATOR DiFRANCESCO: Well, it's an historical renovation.

SENATOR LITTELL: Why don't we call on your two colleagues, first, and then go to the questions and answers.

Jim DiEleuterio, Treasurer-Designate.

TREASURER-DESIGNATE JAMES A. DIELEUTERIO JR.: Treasury would like to express our sincerest appreciation to the sponsors of the bill, who recognize that with the advent of competition in the State's energy markets, energy tax reform is vital to protect municipal revenues and to level the competitive playing field among energy suppliers. This bill will substantially reduce energy taxes for all energy consumers and promote economic development and job creation.

Senate Bill No. 31 comes after more than two years of study of many complex and difficult issues, as well as our extensive consideration of invaluable input received from all affected parties. This process included

discussions with residential and business energy consumers, municipalities, independent power producers, and energy and telecommunication utilities.

Treasury strongly supports Senate Bill No. 31; however, we have some concerns with respect to provisions providing an exemption from the sales and use tax to certain cogeneration, or self-generation, facilities on their purchases of gas and utility services. This tax exemption and related provisions dealing with grandfathering, as set forth in the bill, differ from that proposed by Treasury and the Board of Public Utilities. Treasury and the BPU propose that only cogeneration, or self-generation, facilities existing as of December 31, '95 be so grandfathered.

Furthermore, we propose the volume of purchase gas subject to the exemption be equal to a base level of volume defined to be each facility's average gas purchases from any source over the previous four years. Our rationale is that grandfathering and tax exemption should be minimized to avoid unfair competition.

However, we also recognize that persons owning cogenerators and self-generators made investments in facilities based upon the existing tax code and that those investments should be protected. Treasury and the Board of Public Utilities chose December 31, '95 as the cutoff date for grandfathering. That date was chosen because it was the date that all concerned parties should have been put on notice by the issuance of the *1995 Energy Master Plan, Phase-I Report*, that the State was contemplating major changes in its energy tax policies. That Master Plan report discussed the fact that reform of the energy tax policy was necessary due to the existing unlevel playing field wherein all energy suppliers were, and are currently, not taxed the same. As a result, it is

the position of Treasury and the BPU that all investments in cogeneration, or self-generation, facilities subsequent to December 31, '95 were made with the full knowledge that there would be future changes in energy tax policy to level the playing field. Therefore, we are somewhat concerned with those provisions of Senate Bill No. 31 which determine the amount of natural gas and the utility service that is grandfathered, as well as the date chosen for the cutoff of grandfathering eligibility.

Senate Bill No. 31 grandfathers, or exempts, from the sales and use tax gas and utility service purchases of natural gas by cogeneration, or self-generation, facilities up to an amount used to generate electricity at the facilities' main plate capacity rating as of March 10, '97. The tax exemption applies not only to persons who own the cogeneration, or self-generation, facility in operation on or before March 10, '97, but also to those persons who file an application for an air quality operating permit for future electricity production with the DEP on or before March 10, '97. It is Treasury's position that the use of the December 31, '95 cutoff date to grandfather gas and utility service up to an average level of prior usage is better suited to create a level playing field.

While addressing the issue of grandfathering, Treasury recognizes that there are constituencies seeking amendments to Senate Bill No. 31 to extend the grandfathering benefits beyond those that are currently written into the bill. Treasury will oppose all amendments which seek to extend the application of the existing grandfathering provisions.

In conclusion, with no reservations other than those concerns expressed today, Treasury strongly advocates support for Senate Bill No. 31 and respectfully requests that the Legislature adopts the bill as soon as possible.

Thank you.

SENATOR LITTELL: I thank you, Treasurer.

President Tate.

COMMISSIONER HERBERT H. TATE JR.: Thank you very much, Mr. Chairman and members of the Committee.

Federal and State actions, along with the changing technologies over the past decade, have led to the introduction of competition into the State's energy markets which were traditionally served by regulated monopolies. Deregulation of the State's natural gas markets began in New Jersey in 1984, when the Federal Regulatory Commission opened up the interstate natural gas pipelines. Ten years later, in 1994, New Jersey became the first state to offer competitive natural gas to all of its commercial and industrial customers, and the Board of Public Utilities recently approved three pilot programs to bring competitive options to residential natural gas customers.

On April 30, 1997 the Board of Public Utilities adopted recommendations to the Governor and the Legislature which would open up the State's electricity market to competition starting in October of 1998. Governor Christine Todd Whitman has stressed two major themes during her administration. The first is to cut taxes for the citizens of the State, including her proposal to cut income taxes by 30 percent. The second is to declare New Jersey open for business to promote economic development and job creation.

Senate Bill No. 31, which is cosponsored by Senate President DiFrancesco and Senator Inverso, will support both of these goals and issues that Governor Whitman has stressed.

New Jersey has, as you heard from Senator DiFrancesco, the highest energy costs and energy taxes in the country, with our electricity costs being about 50 percent above the national average, and our energy tax is the second highest among the industrial states that were surveyed. New Jersey's high energy costs and taxes, however, act as a deterrent to business locating or remaining in the State of New Jersey. This legislation, combined with the Board of Public Utilities' efforts to introduce competition into the State's natural gas and electric power industries, represents a significant step toward lower energy bills for all the State's residents and businesses. It will ensure that both energy taxes and rates will go down. Lower energy rates will help make New Jersey more attractive to business considering expanding and moving into the State.

Existing energy tax policies were developed over a century ago in an era that contemplated natural gas and electricity being provided by regulated monopoly utilities. Existing energy tax laws result in utility and nonutility suppliers of natural gas and electricity being taxed differently. Increased competition has led to a growing concern regarding differences in the way that utility and nonutility suppliers of energy are taxed. Differential tax policies that favor one entity over another in a competitive marketplace could lead to unfair competition and compromise economic efficiency, which would lead to higher prices for the State's energy consumers.

Significantly, the differential tax policy has led to a decline in the State's collection of gross receipts and franchise tax revenues that are distributed to the municipalities. This decline occurs as customers switch to nonutility suppliers of energy, since utility customers must pay gross receipts and franchise taxes while nonutility customers do not. In New Jersey's Energy Master Plan Committee, they recognized these concerns in its 1995 report and recommended that the Board of Public Utilities and the Department of Treasury form a joint task force to investigate these and other related issues.

The joint task force, after an extensive, open process for nearly two years, included public workshops and three public hearings across the State, developed proposed modifications to the State's energy tax policies. The proposed legislation which is before you, generally consistent with our recommendations, will cut energy tax rates at approximately 45 percent over five years for each household and business currently receiving natural gas and electric utility service; require that 100 percent of all of those reductions in energy taxes be passed through to residential and business customers to lower their energy rates.

This will result in all customer rates going down by about six cents on the dollar. It prevents future erosion of gross receipts and franchise tax revenues to municipalities due to increased competition in the natural gas and electricity markets. It enhances economic efficiency by taking competing utility and nonutility entities the same. It stimulates economic development and enhances the State's ability to attract and retain jobs.

In the natural gas industry, competitive reform took place prior to changing tax policies, and this has led to the current situation where nonutility

suppliers of natural gas have roughly a 13 percent price advantage over utility suppliers, since nonutility suppliers do not have to collect the gross receipts and franchise tax. Not surprisingly, many nonutility suppliers are offering discounts in and around the range of 13 percent. Nonutility entities currently supply retail customers with over \$230 million worth of natural gas per year. This has led to the State losing over \$30 million per year in gross receipts and franchise taxes that would have been collected had the gas been supplied by utilities.

Last year the State collected over \$1.1 billion in energy gross receipts and franchise taxes. Over \$875 million, or 75 percent of this amount, was collected on electricity sales. On that basis, the Board of Public Utilities believes it is critical that energy tax policies be modified before the electric markets are opened to competition. If not, the amount of gross receipts and franchise taxes lost due to competition in the electricity marketplace will dwarf the amount lost due to competition in the natural gas marketplace.

The Board of Public Utilities, in its recommendations on the restructuring of the electric power industry, has called for near-term rate reductions from 5 percent to 10 percent for all customers commencing in 1998. The Board clarified its initial proposal to require that the reductions are off of existing rates, thereby, preventing utilities from first raising rates prior to lowering them. The Board clarified that total rates to customers be lowered and would be offset by any stranded cost charge resulting in real rate reductions to all customers.

The proposed energy tax policies would reduce customers' energy tax rates from about 13 cents on the dollar to 7 cents, and this 45 percent

reduction would reduce customer rates by about 6 cents on the dollar, or 6 percent. When you combine both the energy tax proposal with the restructuring proposal, the two proposals together will give customers a combined reduced rate between 10 percent to 15 percent.

Since the bill requires 100 percent of any tax reductions be passed through to customers, this is truly a tax break for the State's residential and business customers and not for the utilities. This will assist New Jersey in attracting jobs.

At this point, I will conclude my remarks. There are other remarks in my written testimony, but that has been supplied to the members of the Committee, and I will be here to answer any questions that you might have.

SENATOR LITTELL: Thank you, President Tate. Let me just clarify one thing. Is there a difference between the sponsors' position and Treasury's position on the grandfathering date, you wanting March of '96, and they want December 31, '95?

SENATOR DiFRANCESCO: I believe that in our legislation, we moved it to '96.

SENATOR LITTELL: Can you tell us what the difference means?

SENATOR DiFRANCESCO: Well, there are a number of businesses -- small businesses -- affected by that, but in consultation with the Assembly sponsor we chose to be more inclusive, I thought. As my recollection, we chose to be more inclusive by moving that date to '96, as opposed to '95, in terms of who should pay. We think the playing field will be more level if it's '96 than it would be if it were '95. That was my

understanding. It wasn't my amendment, but I think that was my understanding of the Assemblyman's position.

SENATOR INVERSO: It was brought to our attention that there were some entities that had made commitments to go into cogeneration, you know, inside-the-fence operations -- one that stands out in my mind is Princeton University -- that basically made a commitment, that had things underway, and they do not have the investment in the ground, as it were, but everything had been in motion, and, in discussion with Assemblyman Bagger and others, felt that it was fair to recognize that major decisions and major commitment of resources had been made to proceed along this path, and that to arbitrarily select a date of December '96, in essence, cut them off, was not the equitable thing to do, and that's why the date was extended.

SENATOR LITTELL: In other words, somebody like Princeton University, who had already contracted for a cogeneration facility, would not gain the benefit the capital investment warranted?

SENATOR INVERSO: Right.

SENATOR LITTELL: What do you have to say about that, Mr. Treasurer?

MR. DiELEUTERIO: Well, Mr. Chairman, I want to make clear that from my testimony, I hope I didn't imply that you think we have a strong difference of opinion here. All I was trying to point out was that there were some differences in how the bill was introduced versus what Treasury and BPU had recommended. The Senate President, of course, is absolutely correct that to choose a date in '96 versus '95 is more inclusive. Again, I just wanted to

point out that there were differences in what the recommendations originally were.

I don't view this as irreconcilable differences. We still strongly support the bill. We'd like to see it go forth.

SENATOR KYRILLOS: Mr. Chairman.

SENATOR LITTELL: March of '96 it is.

Senator Kyrillos.

SENATOR KYRILLOS: That's why you call him Mr. Consensus, right?

SENATOR LITTELL: Right.

1997, that's the way it will be. At least coming out of this Committee.

Senator Kyrillos.

SENATOR KYRILLOS: Just a quick remark, Senator. Our congratulations to the Senate President and Herb Tate and the Treasurer's Office and everybody that worked on this bill, because our part is easy at this point. I know there has been an enormous amount of work that has gone into this, enormously contentious issues, complicated issues, lots at stake, and having wrestled with some of these energy deregulation issues myself in the past, I know how hard it can be. And while there may be some quibbles in this testimony that we hear today and people may have some real concerns, by and large, almost everybody is going to come up here and support this effort, and that's not by accident. I know there has been a lot of work, painstaking work, to glue this whole thing together. It's absolutely essential that we move forward as fast as possible because of the changing energy marketplace

landscape, both for economic development reasons and to level the playing field amongst all the players and protect municipalities insofar as property tax relief is concerned. So I applaud all the players.

Thank you, Mr. Chairman.

SENATOR LITTELL: Thank you, Senator Kyriilos.

Senator Inverso, do you want to say anything as cosponsor?

SENATOR INVERSO: No, I'm fine.

SENATOR LITTELL: Thank you, gentlemen. You may stand down.

SENATOR DiFRANCESCO: Bob, if I could only just emphasize that I know you are going to hear from lots of people on this issue, on different points on the issue, but as you know, because you were here when we first talked about it to the Conference of Mayors, I don't think there should be any speculation about the municipal aid revenues being available. I think you and I and Pete and Joe and everyone else involved agree that the bills, although separate, are a package, and our primary -- as legislators, one of our primary concerns, if not the primary concern, is making sure that the municipalities continue to receive as much money as possible, and I believe that Pete's bill has been drafted accordingly.

I just don't-- You know, I'm frustrated by things that I hear and read about, whether or not the money is going to be available and things like that. That's a budget priority as far as we're concerned, and I want you to continue to emphasize that, if you don't mind.

SENATOR LITTELL: I don't mind. There is a poison pill in that that-- (indiscernible) Certainly, if anybody has anything to say, we're not going to tell them they can't speak, but that's another bill for another day.

I just have one question that I would like to ask -- two, really.

Herb Tate, you and I were at a meeting together, and I spoke about the possibility of prohibiting out-of-state utilities that want to sell gas and electric in New Jersey to our large market, unless they do something to clean up the air in their own states. Have you done anything about that?

MR. TATE: Yes, Mr. Chairman. In the Master Plan report that we issued on April 30, 1997, we took the lead from the Governor in calling -- that the EPA would try to adopt the more stringent air emission standards that they proposed in the beginning of this year. Those new, more stringent air pollution control standards impact, most severely, in the Midwest where a lot of the cheaper coal, fossil fuel plants really stand to benefit and gain from opening up these new markets in the Northeast. If those standards are adopted and go into effect, obviously, they have to adopt higher and more stringent pollution control measures to clean up their plants to come into the State of New Jersey.

At the same time, if that strategy is not totally successful, Commissioner Shinn is now negotiating with the OTAG group -- that is a group that was formed between the midwestern and the northeastern states of all the environmental commissioners -- to come out with a regional standard for air emissions that would, again, have the impact on the midwestern states to do more cleanup of their power plants and, at the same time, to try to establish an emissions trading program -- a cap-and-trade program -- in which,

if a portfolio of generation capacity was to be marketed and tried to be sold in a State like New Jersey, (a) they would have certain minimum standards that they would have to meet through that emission portfolio standard, and second, they may be required to buy emissions credits; that is, there would be a cost of doing business if they were not able to meet the more stringent standards here in the State of New Jersey. Therefore, we would hope that that kind of a trading program would lessen the competitive advantage that they would gain by having dirtier plants.

Finally, we have indicated that there should be, in the Master Plan, from every generating supplier that comes into the State, disclosure of where their generation supply is coming from -- that is, what type of plants are they going to be sending this power from, what are its emission standards, does it meet the Federal guidelines, does it meet our State requirements -- so that consumers will know whether they want to shop for dirtier, cheaper power or whether or not they want to make a decision and say, "We would rather have power that is going to be more environmentally sound."

We think that with those three proposals right now, we are in a good way of trying to levelize the playing field and try to deal with not causing any more problems for our air emissions problems here in the State. But the stationary sources, Senator, as you have indicated over the last couple of years, is the second biggest contributor to our air pollution problems here in the State.

SENATOR LITTELL: Thank you. The other question is, what are you doing to encourage our utilities to move into the hydrogen phase of energy sales for industrial and commercial uses? I realize not every facility, at the

outset, would be suitable to use hydrogen in, but it's a fuel that is going to be necessary to use in the future, and I just wonder what we're doing in New Jersey to foster that?

MR. TATE: Do you mean hydroelectric power?

SENATOR LITTELL: No, hydrogen.

MR. TATE: Hydrogen?

SENATOR LITTELL: In replacement of natural gas.

MR. TATE: Sir, I'd like to, if I could, have an opportunity to get back to you on that one. The natural gas and the hydroelectric I'm familiar with, but the hydrogen technology, if you give me an opportunity, I'll give you a response to that question.

SENATOR LITTELL: Thank you.

Thank you, gentlemen. Would you stand down please, so we can get on with the testimony.

Staci Berger, New Jersey Citizen Action.

S T A C I A. B E R G E R: Good afternoon.

SENATOR LITTELL: Press the button so the red light is on.
(referring to microphone)

MS. BERGER: It looks like an electrical-- There we go.

Good afternoon. My name is Staci Berger, and I am the Energy Organizer for New Jersey Citizen Action, and I appreciate the opportunity to speak to the Committee today. We're the State's largest independent citizen watchdog coalition. We represent 60,000 family members and over 85 affiliated tenant, senior, and religious organizations. We've been monitoring this, as well as the other energy issues around the State, very closely.

We feel that S-31 and its counterpart, S-30, meet at least the minimum guidelines of fair and equitable energy taxation, given the changing marketplace. We are, however, cautious of the claims made by Governor Whitman and the rest of her political appointments that these taxes will result in real significant and meaningful reductions in the energy bills of New Jersey ratepayers, particularly residential and small-business customers.

As participants in the Master Plan proceedings which culminated last month in the final order that President Tate spoke about, NJCA was one of the strongest voices for lower rates for New Jersey's residential and small-business customers.

In my work, I speak to groups of tenants, workers, senior, and low-income residents, and their message has all been the same. They need lower rates and they need them now. We feel that it's positive that S-31 seeks to bring the tax portion of energy bills under control and should create a level playing field for all suppliers and still protect local governments from potential budget bloodshed.

This certainly is no easy task, and we commend you, people who work on this bill, to make that possible, especially Senator Inverso who is familiar with energy and high rates given his constituency in Monroe Township.

SENATOR INVERSO: You had to remind me.

MS. BERGER: I'm sorry.

SENATOR INVERSO: You had to remind me.

MS. BERGER: Well, you know, I've got to do my job. They're watching. They're good people.

With that in mind, I just want to outline the three major portions of Citizen Action's concerns regarding this change and what those changes will mean for rates for residential ratepayers.

First of all, we felt very strongly, and we're glad to see that the Legislature agreed with us, that the elimination of GRFT must not result in an increase of local taxes. We feel that the frozen funding, which is based on the highest aid in the last three years, is certainly a step in the right direction to make sure that the municipalities are not zapped by a tax change. While this funding formula protects local governments from the ever-shrinking pool of revenue, it doesn't account for inflation, and we think there should be a mechanism for review once we go through this, because the numbers that we are looking at are all just forecasts, and we're not really sure what's going to happen -- we don't know when we open the market. We're pleased that this moves away from this administration's policy of lowering one tax while raising another, and we're particularly pleased with the poison pill mechanism that's in the legislation.

Second, we feel that tax changes should be progressive and not disproportionately harm working people. While the elimination of GRFT does not fundamentally alter the reliance of energy revenue on regressive taxation, it is a move in the right direction. By using a corporate tax and applying it to all of the energy suppliers wanting to do business in New Jersey, the proposed legislation attempts to equalize taxation, or at least is a step toward that, between a business and its customers.

Unlike GRFT, which was a complete pass-through to consumers, the use of the corporate tax and sales tax will go a long way to balance that and

shift at least some of the responsibility onto the suppliers themselves. They may attempt to pass through those costs, but in a restructured environment, we think that companies will be unlikely to increase the direct costs to their consumers. We hope, like many other people, that the restructuring of the electric industry will help keep the taxation mechanisms fair and competitive, and we think that this legislation can certainly go to making that happen.

And lastly, we think that the ratepayers must be protected against budget shortfalls in the General Treasury. The TEFA is a commonsense approach to the problem of the original budget gap of approximately \$480 million that was reported last fall. Because TEFA will be phased out over five years, the municipalities will not be shell shocked from an immediate loss of revenue. This means, however, that the real savings to ratepayers that has been talked about today will not be fully realized until at least 2003.

It is here, on the question of the bottom line, that we part company with most of the people who will speak before you today. We feel that the people of New Jersey need lower rates, and they need them immediately.

We think it's inappropriate that the BPU and the Treasurer's Office make claims of lower energy bills until we've actually seen what happens when TEFA is phased out. Many people have touted the 45 percent reduction in energy rates as being immediately convertible into a 6 percent reduction in overall rates. This won't be true in this election cycle or even the next one. The proposed changes in GRFT and the promises made by the BPU in the restructuring order will result in a small and perhaps meaningless reduction in

the high cost of electricity in New Jersey, the fourth highest cost around the country.

Senate Bill No. 31, while important and necessary legislation to even out our playing field, is not and cannot be a panacea for high rates. In the last two years, over 15,000 people have signed our petition for a 25 percent rate reduction in electric rates, and we feel that if the Legislature truly wants to give residential and small-business consumers the immediate rate relief that is so desperately needed in this State, that you should mandate this reduction when the final order comes before you, the Legislature, in the fall.

There is no guarantee that eliminating GRFT and this replacement will lead to permanently lower rates for residential or small-business customers, or at least not as low as the rates can be and should be. A conservative estimate of the tinkering and hoop jumping being done by the Board and the utilities in terms of restructuring show a total of 10 percent, maybe 12 percent reduction in rates before the public is forced to bail out our monopoly utilities for their stranded costs. As S-31 moves through the Legislature, our eyes and the eyes of the people of New Jersey are on Trenton to see who will have the political courage to do what is necessary, to do what is right by ratepayers and their wallets, and really bring lower rates to New Jersey.

I'll be happy to take any questions.

SENATOR LITTELL: Thank you very much, Staci.

Are there any questions for Staci Berger? (no response)

MS. BERGER: No, then I can go to lunch. Thank you.

SENATOR LITTELL: Thank you.

Kevin Lynott, GPU; Henry Levari, Atlantic Electric; Bill Walsh, PSE&G; David Klucsik, New Jersey Natural.

H E N R Y K. L E V A R I: Good afternoon, Chairman Littell, and members of the Committee. My name is Henry Levari, and I'm Senior Vice President of Atlantic Electric, an investor-owned utility that serves the southern third of New Jersey -- approximately one million people in southern New Jersey.

Atlantic Electric is a subsidiary of Atlantic Energy, and we're pleased to have the opportunity to participate in this hearing because of the importance energy policy plays in the lives of New Jersey citizens and our customers.

Also, I'm here, along with my colleagues, on behalf of the New Jersey Utilities Association. The NJUA formed a task force, which I chair, and we spent considerable time working with the Treasury and the BPU analyzing this issue over the last couple of years. We do fully support this legislation.

In a few minutes, I'll introduce the members of the NJUA task force who will speak on behalf of the bill.

Let me begin by stating that Atlantic and the NJUA agree with the Energy Master Plan findings that, with the advent of a competitive energy market, changes are required to New Jersey's energy tax policy.

Currently, utilities pay approximately 13 percent of their total revenues to the State Treasury in the form of a gross receipts and franchise tax. The State then distributes a portion of this tax to the municipalities. Under the current law, nonutility energy providers and utilities located outside of

New Jersey are not required to pay the gross receipts tax, and this has resulted in less taxes being collected, especially for the deregulated gas market.

With the advent of retail electric access beginning in October 1998, New Jersey energy users will be able to purchase electricity from many providers other than the State's utility companies. Under current law, these energy purchases will not be subject to the State gross receipts tax, therefore, current New Jersey energy tax policy is not changed. The State and the municipality will be adversely affected by these lower collections.

We support Senate Bill No. 31 because it will lower the New Jersey customer gross receipts tax burden by approximately 45 percent when this is fully implemented. This will also help promote economic development. It will also help provide fair and equitable competition by taxing utilities and nonutility entities in the same manner, while ensuring no further erosion of energy tax revenues for municipalities.

We agree with the bill's approach to substitute the gross receipts tax with a sales and use tax of approximately 6 percent, also a 9 percent corporate business tax on net income, and a transitional energy facility assessment, which will make up the difference in the first year and then phase out over a five-year period.

The bill's sales tax approach is a giant step in the right direction because it helps to assure that all energy users pay their fair share of the tax obligation. It's well known that surrounding states have lower energy taxes than New Jersey, and this gives them a competitive advantage. Therefore, it is imperative that the transitional energy facility assessment be phased out as soon as possible.

Healthy, vibrant municipalities attract and retain businesses and therefore are the foundation for economic development. It is essential that we all continue to support their efforts. We are pleased that the companion, Senate Bill No. 30, ensures continuing compensation to the municipalities for hosting utility facilities.

Atlantic Electric and the NJUA support the tax goals of fairness, economic efficiency, competitiveness, stability, simplicity, and comprehensibility. Senate Bill No. 31 meets these goals without imposing any new local fees, taxes, or other assessments on public utilities.

Finally, let me emphasize that we believe, as New Jersey approaches a competitive energy marketplace, the tax policy of the State will affect the State's ability to compete. Therefore, the energy tax policy must change to help the State compete in the regional and global economy.

Thank you for giving us the opportunity to participate in this process. And now I'd like to introduce my colleagues, who will speak on this bill and then will be available to answer questions.

Our first speaker is Kevin Lynott, from GPU Energy.

KEVIN LYNOTT: Thank you, Henry.

I have copies of my testimony. I won't read it, but I will paraphrase it.

As Henry mentioned, my name is Kevin Lynott. I'm the Manager of Government Affairs for GPU Energy. We're here today to support S-31. If it passes, it will dynamically change the way energy is taxed. We've worked for over a year on this legislation through many meetings and drafts of the legislation. We have worked out our original concerns. It's very workable for

us. We look forward to its passage, and the time is right. The paradigm shift taking place in New Jersey, the choice, is coming; we need to change the tax policy to make sure we have a level playing field.

This bill, as you've heard, does many things: reduces the tax rate 45 percent, stops the erosion of the tax revenues. It gives economic development a significant boost. It creates a consistent tax policy, and it's a stable source of funding for municipalities.

We're very pleased at the way that this legislation has been developed. I have additional comments, which you can read. That's all of my prepared statement. If you have any questions, I'll be glad to answer them when we finish.

MR. LEVARI: Thank you, Kevin.

Our next speaker is Dave Klucsik, from New Jersey Natural.

DAVID KLUCSIK: Thank you, Henry.

Good afternoon, Mr. Chairman and members of the Committee. My name is David Klucsik, and I'm Vice President for External Affairs at New Jersey Natural Gas Company.

New Jersey Natural provides natural gas utility service and related energy services to more than 370,000 customers in virtually all of Monmouth and Ocean Counties and parts of Morris and Middlesex Counties. The company or its affiliates also provide competitive gas and related services to wholesale customers in 17 states.

I'm pleased to appear before you today, because we believe that S-31 is truly landmark legislation. It will become part of a framework for a robust, competitive energy market in New Jersey. And let me add that reform

of the State's energy tax structure is, indeed, a prerequisite for competition among utility and nonutility energy vendors.

To understand the evolving competition in New Jersey's energy markets, it's instructive, I believe, to review the history of natural gas deregulation. Most of its history is just that, it's history. This is because deregulation of natural gas markets began in the mid-1970s and is continuing, as you know, today. Much can be learned from the natural gas industry's evolution from wellhead price controls and interstate pipeline monopolies to last month's introduction of residential competition among utilities and energy marketers serving residential customers in New Jersey Natural Gas Company's system.

In that time period, since the mid-'70s, competition has brought lower prices and competitive services to industrial and commercial markets, and that competition is stiff. In NJNG's service area alone, more than two dozen energy vendors are serving more than 2000 commercial and industrial customers who formerly purchased gas only from New Jersey Natural. Those customers generally represent larger volume consumers and sophisticated energy buyers.

The competition has not stopped with big customers. Last month, New Jersey Natural opened its Natural Solutions Pilot Program, bringing new choices of suppliers, prices, services, and contracts to residential customers. We had planned a two-month open enrollment for up to 5000 residential customers on a first come-first serve basis. I'm pleased to report that the pilot's first phase was fully subscribed in just 16 days -- not two months, as we

had expected, 16 days -- an indication of consumer interest in deregulation benefits.

Let me point out here that NJNG is currently -- there is generally indifference as to customers' migration to third-party energy providers. This is because utilities earn no profit on sales of the gas commodity. Instead, we earn on our delivery service, which remains, regardless of who supplies the molecules of natural gas.

While utilities are indifferent, the State of New Jersey is not. Many of those thousands of customers of all sizes who have switched did so purely on the basis of price. Utilities charge 13.5 percent gross receipts and franchise taxes, and others do not. The result as the deregulated markets grow, State energy revenues shrink.

Keep in mind that a more competitive market is already here for natural gas. At New Jersey Natural, we believe customers of all sizes are benefiting and will benefit from deregulation, but clearly, the State Treasury may not, and the State's utilities could be forced to yield much of their customer load to others without even much of a fight, even where customers want to stay with their traditional bundled utility service. That's not a policy, we believe, for robust competition.

Many policy makers have debated whether the residential customer, the so-called little guy, will ultimately benefit from deregulation. We believe they will, and our experience so far provides strong evidence that they will. The maximum benefits for the little guy, however, can only be achieved through your enacting S-31, and we urge your support.

Thank you. I'll also be available for questions.

MR. LEVARI: Our last speaker is Bill Walsh, from Public Service Electric & Gas.

WILLIAM J. WALSH JR.: Thank you, Henry.

Mr. Chairman, members of the Committee, and staff, I'm Bill Walsh. I'm with PSE&G, and I thank you for the opportunity to present PSE&G's position on this legislation before you, legislation that represents the culmination of about two and a half years of work, a bill that is fair and probably will be supported by nearly all of the folks who will come up and testify before you this afternoon. We compliment the Senate President and Senator Inverso for their leadership in moving this issue forward with the knowledge that the tax inequities need to be resolved prior to retail competition in the electric business in the State of New Jersey.

We do have a couple of concerns, based on testimony we heard when this issue was discussed before the Assembly Policy and Oversight Committee just a few weeks ago. We had believed that after two years of negotiations and discussions that the major parties had reached agreement on the concept of the bill and the major positions that would move forward. However, we've heard some requests for additional changes that clearly go beyond technical amendments and technical adjustments and really fall in the realm of policy changes. Two issues are of particular concern.

As you are aware, the cogen community now enjoys tax exemption on the natural gas they purchase to generate electricity for behind-the-fence projects and do not pay on that energy -- the electricity generated either. We agree that existing plants, which represent investments made in another time

and under a different set of regulatory rules that allow for the tax subsidy, should retain that tax exemption on the natural gas that they purchase.

Going forward, however, this bill requires that new projects -- for all new cogen projects, it would be required to pay the natural gas tax -- the 6 percent sales tax on the natural gas that generates that electricity, maintain that exemption on the electric behind-the-fence, and we believe this to be a fair proposal. However, we are hearing requests for continued tax exemptions for all new cogeneration projects as yet unplanned and not even on the drawing board at this point in time.

We believe that continuing that exemption provides an unfair competitive advantage for certain cogen projects, an unjustifiable tax subsidy for a technology that is no longer new, a technology that does not require subsidies to compete, in fact, may even be outdated in the future.

Our other area of concern is the desire to wheel electricity between cities and sites across the State tax free. It was raised in prior testimony, with reference to the term "site" in the bill, that certain facilities might lose their tax free status because of right-of-way or a street runs through their property. This is clearly not the intent of the legislation.

PSE&G agrees with the intent of the bill with respect to the term "site" to permit existing cogen plants to supply power to facilities that may, in fact, be across the street from the plant generating the electricity but which are clearly part of a single-site or a single-corporate location. However, we would strongly oppose any attempt to amend that definition to broaden it so that tax free energy could be wheeled between cities and between multiple sites and multiple locations throughout the State of New Jersey.

Broadening that definition in this manner would also create a loophole which could allow a consortium of businesses to erect a cogen facility and wheel tax free power anywhere, through multiple locations throughout the State. And if we are truly going to create equity for the generators in the electric business as we move forward, then let's make sure that we do that. Modifying this bill and creating these loopholes actually, I believe, undermines the goal of the sponsors -- a major goal to stabilize tax revenues for the municipalities in the State of New Jersey.

We strongly urge the Committee to maintain that spirit of cooperation and commitment as we move forward, the commitment that was crafted over two and a half years in discussions of this issue, and reject the requests to change the bill in this manner in your deliberations.

We believe most of the major policy issues have been addressed in this bill, and it parallels the Master Plan, as you've heard, which is our State's blueprint for choice as we move forward. And PSE&G's message today is that the State, the towns, the municipalities, consumers, and energy industry need this legislation sooner, rather than later, to provide the flexible policy to deal with any transaction in the energy business as we move forward.

You've heard about the electric choice, a little more than a year away-- They've mentioned pilots that are going on in the residential gas market. You've also heard of the announcement of a residential electric pilot -- the Monroe Township pilot, to move forward. If we permit the electric market to open up to competition under the existing tax structure, then the bottom falls out of tax revenue, and we create severe economic dislocations for

the State and for the municipality and, potentially, utility industry jobs, as thousands of customers leave the system to purchase tax-exempt energy.

While the energy policy is poised for the 21st century, the gross receipts and franchise tax methodology is rooted in 19th century economics, and S-31 is the solution to the problem at hand. It provides a forward-looking tax policy, it's balanced, it's fair, and it's flexible enough to handle any transaction in the business; and the time to do that is now because competition is not in the future, it's here. States around us are revising their energy policies. The majority of the states throughout the country are reviewing the entire electric business and will allow choice -- if not totally, but certainly in part, by the turn of the century.

This is a major policy change before you. In the six months between now and the January 1, '98 effective date of this legislation -- is certainly not an unreasonable amount of time to expect for all the changes that are necessary, to refile all the tariffs, to get Board review and approval to put this in place by January 1.

A hallmark of this legislation, Mr. Chairman, is the establishment of similar tax liabilities for similar transactions in the business. So we ensure that as consumers make choices in energy, they make them based on what makes the best economic sense, the most efficient sense, and not who can cook the books and come up with the best tax avoidance scheme.

My testimony includes some numbers and examples that will show you, under the current tax policy, how much an industrial customer for a utility pays for taxation per megawatt of power. It also includes figures that show you our estimates of what a cogeneration customer pays and what a

utility customer will pay under the new revised tax policy. It shows that clearly, there is still a significant advantage to those who would cogenerate behind the fence.

Despite this disadvantage, we clearly believe that this legislation represents the most equitable compromise that can be reached short of charging taxes on the electric output of cogeneration. It strikes a careful balance that still provides them with a significant advantage but really levels the playing field to the extent possible and practical at this point.

With the more balanced tax proposal that we see under S-31, we start to narrow the margin between utility and nonutility generation. And we believe that the workers in the generating stations owned by utilities will see a fairly set out policy, one that honors the commitments made to those who made investments under a different set of rules, that going forward fairly requires all suppliers and consumers to bear their fair share of energy taxation, and provides them with the opportunity to hold their jobs in an open market by removing taxes as an economic advantage from one source over another.

We hope you will carefully consider the balance struck by this legislation. PSE&G is pleased to support the bill in its current form, and I thank you for your cooperation and attention. This concludes my remarks.

MR. LEVARI: Mr. Chairman, that concludes our testimony, and you can tell from the comments that NJUA and its individual utility members are supportive of S-31. We're available for any questions.

SENATOR LITTELL: Thank you very much, Henry.

David, you said that in the natural gas business that people have already switched to another supplier in order to save the 13.5 percent tax. You

also said that this is a good idea because it will reduce costs. The way I see it, it would increase costs for those people who have already left the utilities to buy gas from somebody else, and starting in January of '98, they'll have to pay 6 percent more than they are presently paying. They're not grandfathered in. The grandfathering applies to -- as I understand it, at least -- it applies to cogeneration stations.

MR. LEVARI: Mr. Chairman, you are correct in noting that under provisions of the bill, the disparity of the tax application between utility vendors and nonutility vendors will decrease. In most of the contracts that I'm familiar with that were offered to customers of various classes, especially those residential pilots that were just opened last month, the tax provision of those contracts noted that changes were pending in the Legislature that might reduce the potential savings. In some cases, we would expect that those savings will be almost entirely and purely based on the current disparity between 13.5 percent and those vendors that are not liable for the gross receipts taxes.

Our view of this would be that the market currently is inefficient in this sense and that, as the tax inequities disappear, that truer competition will take place, and competition based on price of the commodity itself, on contract terms, on a number of other factors in bringing gas energy to the customer, including that customer's demand profile, will, in fact, be the more accurate arbiters of the ultimate price or other factors that make one vendor more attractive to the customer than others.

It is true that the cost savings that are currently attributable solely to the gross receipt tax phenomenon will reduce. In some cases, the vendors have promised more than a year contract, in some cases two-year contracts,

with guaranteed savings. Depending on the contract terms, some of those guaranteed savings -- "guaranteed" -- have been hedged with the qualification notwithstanding tax changes.

SENATOR LITTELL: Well, wouldn't that--

MR. LEVARI: Did that answer your question, sir?

SENATOR LITTELL: Wouldn't that make sense for us to maybe phase them in at 1 percent a year to get them back into the system, or should we acknowledge that there is a change and just do it effective January 1 of '98? And as part of that, shouldn't we also take the people who are going to be grandfathered in and reduce that exemption over a six-year period so that the grandfathering is eliminated and everybody is truly on a level playing field? Otherwise, we're always going to have inequities.

MR. KLUCSIK: I think the important point, from a customer's standpoint, is that they must be aware of the changes in advance of their signing a contract. And that's one of the points that we, as a utility, have been making to our customers, is to ensure that all provisions of a contract are well understood prior to signing up with a broker or other vendor to know whether the provisions or the advantages are purely based only on tax consequences or whether they are based on other pricing matters. If the tax inequities go away, the playing field becomes much more level and much more competitive based on the other factors, and we believe that is a more truly competitive field.

I don't believe that a gradual phase-in necessarily serves the customers or the State. The reason for that is because, at this point, the vendors are generally not offering contracts of that length of time, and it's unlikely that they would, depending on, again, the customer's load profile.

Clearly for large industrial and commercial customers, some of whom buy their own gas nationally at this point, they have a variety of contracts that could stand anywhere from three months to three years. In those cases, many of the pricing formulas are hedged in the future's markets so that tax consequences by themselves would probably expire on a relatively shorter life contracts.

SENATOR LITTELL: Well, that's something we're going to have to talk about. I think that the grandfathering ought to disappear after five or six years. I think the people who are going to have to start paying a little more on January 1 maybe ought to get at least two years to phase that in. We could do it 3 percent a year for two years.

It seems to me that has got to be looked at anyway. I don't know all the answers, but--

MR. KLUCSIK: Mr. Chairman, we would be happy to sit down with you to go over those factors.

SENATOR KYRILLOS: Mr. Chairman.

SENATOR LITTELL: Senator Kyrillos.

SENATOR KYRILLOS: Just to follow up on your point-- My microphone doesn't seem to be working. It is true, following up on your concern, that not many people were able to shop around for natural gas. There are pilot programs going on for most residents.

Is that correct, David? (no response)

Maybe private sector folks had lots of choice in the last--

SENATOR LITTELL: Commercial and industrial.

SENATOR KYRILLOS: Yes, but there are some pilot programs going on for residents.

You were talking about commercial people. Is that your concern?

SENATOR LITTELL: Well, they're big users.

SENATOR KYRILLOS: Well, they've been having a nice tax break at the expense of the rest of us for a long time, so I'm not sympathetic to them. I understand what you're trying to say, but I wanted to chime in on that.

MR. KLUCSIK: Senator, if I can comment on the availability of the pilot programs. In our case, our pilot was 5000 residential customers for the first phase. Since it was so quickly subscribed, we are examining both the acceleration of the schedule, as well as the number of customers to be included in the second phase, which we had planned to start in September.

In our case, certainly, you'll see some acceleration of the availability of the pilot. There are a couple of limitations to the pace at which the pilot programs are introduced that have little to do with whether we'd like to provide more customer choice. We would, but there are some realignment of gas supplies that are contracted under a longer term basis for all firm customers, which has to be adjusted along the way, as customers migrate to third-party brokers and third-party pipeline capacity arrangements.

So there are some technical considerations, kind of, behind the bill, if you will, that in part influence the number of customers to be unlevelled, if you will, at any given time. That's why it's more of a gradual phase-in.

Our program, however, was not limited to any class of customers. All classes of our customers have now been afforded some degree of choice. It's been a first come-first serve basis, not limited to geography or consumption.

SENATOR LITTELL: What's your view, Senator Kyrillos, on the grandfathered facilities? Don't you think we ought to eliminate that over a five- or six-year period?

SENATOR KYRILLOS: As it relates to gas, or are you talking about for-- Are you talking about the nonutility players?

SENATOR LITTELL: Under the proposed legislation, it's my understanding that they are exempt from paying any tax on the natural gas that they buy to generate electricity. They're also exempt from charging any tax on the sale of that electricity to their own facility.

Am I right about that?

MR. KLUCSIK: Yes, that's correct.

SENATOR LITTELL: Should that go on forever? Does that create a level playing field? I mean, if you give them five or six years, they can write off most of it in five or six years time.

SENATOR KYRILLOS: What you're saying is, after five or six years time--

Senator Inverso, is that-- The full taxation will kick in at that point. Is that what Bob Littell is describing?

SENATOR INVERSO: I think he's questioning whether or not--

SENATOR KYRILLOS: Is there a time limit on the grandfathering?

SENATOR INVERSO: No.

SENATOR KYRILLOS: No.

SENATOR INVERSO: The Chairman is questioning whether the provision in the bill that provides for grandfathering should, indeed, rather have phaseout.

SENATOR KYRILLOS: It doesn't have a phaseout now, right?

SENATOR INVERSO: It doesn't have a phaseout now. When we looked at this, it was a question of looking at good policy decisions that were made and financial investments made as a result of public policy encouraging that type of investment and whether or not you should pull the carpet out from under those investments at this point in time by changing the playing field.

SENATOR KYRILLOS: So Bob is talking about the grandfathering aspect of this for gas and electric across the board?

SENATOR INVERSO: Right.

SENATOR KYRILLOS: It's obviously a delicate balance.

SENATOR INVERSO: But there is also another issue in terms of the unbundling, where someone has, because of the opportunity to unbundle, went out and purchased the gas, in this case, without making a major investment in that transaction. They went out and just contracted with someone else to supply them the gas.

So you've really got--

SENATOR KYRILLOS: That's a different issue.

SENATOR INVERSO: That's different. There are two different--
The Chairman is asking whether--

SENATOR KYRILLOS: And they're not grandfathered, though.

SENATOR INVERSO: No, the tax would be imposed. What the Chairman is saying is, in the case where you've had unbundling, maybe there ought to be a gradual phase-in of the tax and where you've had the cogenerators, you know, the inside-the-fence operations, maybe there should be a phaseout.

I think that's what he is proposing.

SENATOR LITTELL: I'm just trying to get it out while there are people here who can comment on it.

SENATOR INVERSO: Maybe that should be addressed by the speakers as to the--

SENATOR KYRILLOS: Well, you asked me my feelings, Mr. Chairman, and I guess, for the natural gas side, that is relatively new and recent phenomena, where there has been choice. It's just that it's new, and there haven't been long-range business decisions made. It's kind of a windfall, if you will, for those who have had the opportunity to have a choice, and most residents haven't had that opportunity, I would add.

But on the other matter of the winding down of the grandfathering, it's an issue that we can't really solve, I don't think. I think that the proponents of this measure -- and we all ought to be proponents -- the sponsors, the advocates have wrestled with this thing, and this very tenuous coalition of support begins to unravel if we get into those issues.

SENATOR LITTELL: Well, I don't think it unravels, Joe, but what you're talking about is--

SENATOR KYRILLOS: Wait til you get to the next round of testifiers.

SENATOR LITTELL: Princeton University should be grandfathered in, because they made a substantial capital investment. The result of that is that they're not going to contribute, because they're grandfathered. But after having a facility on-line for five or six years, they recaptured most of their capital investment, and maybe they ought to be treated like everybody else at that point in time.

In the meantime, somebody who is running one of these utilities -- one of these representatives out here -- was selling electricity to them, and we were getting 13.5 percent tax on that. We lost out. They lost out, and the only people that benefit from that deal is Princeton University. And I'm not against them doing that, because we've advocated that, but it shouldn't go on forever. It should not go on forever.

I don't know whether five or six years is--

SENATOR KYRILLOS: It's not just Princeton University, but it's all the cogenerators heretofore, right?

SENATOR LITTELL: Well, that's the example we were talking about here earlier, for the change in the date. I just think we ought to have some input from all these folks in the utilities.

You certainly can tell us better than we can how long it takes a company or a college or a university to recapture their investment, and shouldn't they be on a competitive playing field with the rest of them?

MR. WALSH: Mr. Chairman, I can tell you that when public utilities invest in generating capacity, we get the money back over four years. It's certainly a different ball game when you look at a private corporation

investing their own funds or having a developer build a project for them on their property.

This was a tough one for PSE&G, but we recognize that, quite frankly, a lot of different institutions -- corporations, large manufacturers, employers in the State, and universities, as we're discussing now -- put up their own money based on a set of rules that were in place that gave them a tax subsidy.

And what we're suggesting is what our compromise portion of this bill is, that beyond those commitments that were made in the past that you recognize that they spent their own funds under a different set of rules and gave them those tax subsidies, and that you grandfather that class but make the distinction, as we move forward, that for all new developments -- you're on notice now -- that you'll be liable for the natural gas -- paying a tax on the natural gas that you will purchase to generate electricity for your facility, so that now that gets back into your economic analysis now as to whether or not cogeneration or some other alternative power production source makes sense to you in the future.

And to those, under the bill, who purchase natural gas off utility systems prior to 12/31/95 will see a tax imposed upon them phased in over a number of years. I think that phase-in period is pretty consistent with the phaseout period of the transitional energy facility assessment, so that as the 6 percent increment comes up on the natural gas purchases, you also get a 6 percent decrement, or decrease, on the electric side of your bill. So it ought to balance out, and I believe that probably 99 percent of the customers benefit with the -- or at least turn out as good as they are now with the new system

after the final transitional assessment is phased out, because then you get the benefit on both the electric and the natural gas consumption.

SENATOR LITTELL: Okay, that's enough of that.

MR. LYNOTT: Senator, if you recall, I think it was Richard Van Wagner -- Senator Van Wagner -- who originally provided the exemption on natural gas for cogenerators. That was certainly done at a time when the industry was developing, and it's a mature industry now. I would agree with Billy Walsh. Going forward, I don't see the public policy reason why to continue the gas exemption for cogeneration.

SENATOR LITTELL: Thank you, Kevin.

Thank you, gentlemen. If there is nobody else who has questions, we'll see you again, I'm sure.

Bill Potter, General Motors, United Auto Workers.

BILL POTTER, ESQ.: Good afternoon, Mr. Chairman. My name is Bill Potter. I'm an attorney with the law firm of Potter and Dixon, and I'm here representing General Motors, which in turn is represented by Thomas J. Noble, who is going to deliver a statement here to you.

It's also my pleasure to have with us a representative of the Tosco Bayway Refinery, Mike Karlovich, who is also going to make a statement.

We are sort of together, Mr. Chairman, because we're together on a very similar issue of importance to this Committee. Mr. Noble will go first, if that's all right.

THOMAS J. NOBLE: We're having a little trouble with the electronics here, sir. (referring to microphone)

SENATOR LITTELL: If the other mikes have a red light on them, shut them off.

MR. NOBLE: General Motors Corporation welcomes this opportunity to present a statement to the Budget and Appropriations Committee on this important legislation. My name is Thomas J. Noble, and I am the Manufacturing Engineering Manager for the General Motors Truck Group Plant located in Linden, Union County.

By way of background, General Motors is the owner of three major manufacturing facilities in New Jersey: GM's Delco Battery Plant in New Brunswick; GM's Delphi Interior Plant located in Ewing-Trenton; and the GM Truck Group's Assembly Plant located in Linden.

These three plants provide 4000 full-time jobs with an annual payroll in excess of \$200 million and pay many millions of dollars in local and State taxes, as well as locally purchased services.

By far the largest of these is the Linden Assembly Plant. This facility has been in operation since 1936. Linden Assembly currently produces the Chevrolet Blazer and S-Series pick-up truck and the GMC Jimmy and Sonoma pick-up. It competes in the most competitive vehicle market in the world today, sport utility vehicles and small pick-up trucks.

The Linden Plant currently provides 2700 full-time jobs in Union County, including 2500 members of the United Auto Workers, down from a high of 6000. Yet even at this reduced level, the Linden Plant is one of Union County's major private employers, and we aim to keep it that way, if we can.

Unfortunately, Linden's future in the 21st century is threatened by a combination of factors. This plant could be closed in the year 2001 when

the run of the current product line is scheduled to end. No new product line is now planned to replace it. Whether or not GM allocates Linden a new product line depends on our ability to get cost, quality, and operating performance in line with the competition, competition which comes not only from foreign producers, but from other domestic assembly plants that pay 50 percent less in utility rates than GM Linden. Our workforce understands the competitive challenges we face, and we continue to work jointly with the United Auto Workers to improve our operation.

Some of the plant's recent accomplishments include: best quality performance of all GM Truck Plants in 1996; one of the most improved assembly plants for labor productivity in North America as measured by the Harbour Report; and a competitive labor agreement reached without the threat of a strike.

As you can see, the Linden team is working hard to earn the right to build a product in the 21st century.

Unfortunately, one of the problems facing the Linden Plant is our 1936 vintage power plant, a facility that produces steam and compressed air for the assembly process. This facility is antiquated and has been kept in operation only because of the extraordinary efforts of our operating engineers. It burns heavy Bunker C oil, and it has to be replaced to meet Clean Air Act standards. Also, it is subject to sudden breakdowns, and if it goes down, the assembly line comes to a screeching halt.

We have been investigating various scenarios for its replacement since 1989. Some of those scenarios include: building a large cogeneration plant with sales to others; having PSE&G overhaul or replace our existing

power plant and run it for us; joint venturing on a project with another manufacturer in the area; and finally, building a small, inside-the-fence cogeneration plant.

We settled on the fourth option and plan to build a small, inside-the-fence cogeneration project. In an effort to be competitive and not tie up GM's capital with this type of project, we signed an agreement with the Quixx Corporation of Amarillo, Texas, to develop a small, 25-megawatt cogen plant, strictly for the Linden Plant's use. Ground breaking for this plant, which will pump an immediate \$20 million into the economy, was scheduled for June 1997, but it may be put off again and even indefinitely.

When PSE&G was not awarded the contract to build or overhaul the GM Linden power plant, PSE&G began to oppose our efforts at every step. PSE&G representatives made repeated offers to GM Linden to dissuade us from building the Quixx-GM cogeneration project. We listened to their offers of flex rates and a new powerhouse, but after analysis, none of them were as competitive as the Quixx proposal.

In 1995, when GM and Quixx filed for review of the cogen plant at the Board of Public Utilities, PSE&G opposed us at every step and helped to delay the ruling for many months. Then, after the BPU ruled in our favor, PSE&G filed their departing load tariff that could force GM to pay PSE&G for the electricity that the Linden Plant produces for itself and no longer buys from PSE&G. We estimate that the bill for these nonpurchases could total \$3 million a year, paid to PSE&G for the privilege of not buying its product. This departing load tariff has been pending at the Board of Public Utilities since

September 1996, over eight months, even though General Motors and other companies filed motions last fall to deny the PSE&G tariff.

On April 17 of this year, the BPU voted to review the tariff as a generic matter. While we applaud every effort by the BPU to conclude this matter, the BPU's vote looks to us as if it will lead to more delays and more uncertainty.

The simple fact is that GM Linden cannot tolerate this situation continuing on much longer. While we understand the issue of stranded cost that is currently being discussed at the BPU Energy Master Plan hearings, the fact of the matter is PSE&G is attempting to invoke a retroactive tariff upon us.

We know of no other cogeneration project in this State that has faced this type of economic disincentive. We are simply a victim of timing, in that our project has been tied to the discussions currently going on regarding stranded cost.

The bottom line is GM Linden needs a new power plant now. The cogeneration process is the vehicle that gets us there, and the use of third-party financing and operation makes the project attractive to General Motors. Uncertainty over when or, perhaps, whether this small cogen plant is built is a direct threat to the Linden Assembly Plant and all of its 2700 jobs.

When I testified before the Assembly Policy and Regulatory Oversight Committee on Assembly Bill No. 2825, Assemblyman Bagger was so appalled by PSE&G's actions that he stated his intention to amend the bill to outlaw departing load tariffs. We hope the BPU has the wisdom to rule

favorably on our Emergent Motion for Reconsideration and will dismiss us from this retroactive tariff.

With regard to the legislation at hand, General Motors wishes to express its qualified support for this legislation which is intended to reduce electric and gas costs by substituting the 6 percent sales and use tax for the 12.5 percent gross receipts and franchise taxes. However, please understand that reducing utility taxes does nothing to benefit the GM Linden Plant and its workforce. That's because GM must -- I repeat, must -- replace its existing power plant with the proposed cogeneration project. Amendments to this legislation are needed to allow this project to go forward and thereby give Linden a fighting chance to survive into the 21st century. We have identified four such areas for amendment which are as follows:

First, an amendment is necessary to prohibit the departing load tariff which will prevent PSE&G from demanding payment for electricity which Linden will not purchase and will not use. If the BPU will not act promptly on this antibusiness, antijobs tariff, then the Legislature must do so.

Secondly, an amendment is needed to exempt the energy output from the cogen plant from the 6 percent sales and use tax on all electricity and thermal energy we produce for ourselves. It would make no sense to tax meals prepared at home to help out the restaurants. So, too, the Legislature should not tax energy that is homegrown at the GM Linden cogeneration plant.

Third, an amendment is needed to prevent the taxation of the natural gas purchased for use in the cogeneration process. Cogeneration gas has been exempt from taxation since the mid-1980s, and we believe that this exemption should continue. Due to the high energy conversion efficiencies

and positive environmental benefits, cogeneration projects make sense both economically and environmentally.

Fourth, we seek an amendment to grandfather the GM facilities from the new 6 percent tax on natural gas purchased for process use at our three New Jersey operations.

The first three amendments address the cogeneration issue. Regarding the proposed fourth amendment, it is important to recognize that the planned substitution of the 6 percent sales tax on natural gas for the 12.5 percent gross receipts and franchise tax will not benefit the GM facility or any other GM plants. For us, this is a tax increase, not a tax cut. Unless the bill is amended, it will raise GM's taxes and the cost of doing business in New Jersey by hundreds of thousands of dollars. The reason is that GM does not purchase its natural gas from public utilities subject to the gross receipts and franchise tax. GM buys gas on the open market at the most competitive prices.

The ability to shop around has been an important part of our competitiveness program. Imposing a 6 percent tax on these purchases does not level the playing field for GM, and, in fact, it will make us less competitive with our counterparts in other states. It increases our energy cost in a State where energy costs already exceed the national average by 50 percent.

Section 28 of Senate Bill No. 31 has a very limited and, we believe, unworkable grandfathering clause for these process gas purchases. We feel that the fairest, simplest way to approach this problem is to grandfather each site where gas has been purchased without paying tax.

In conclusion, again, I wish to express General Motors' appreciation to the Committee. The GM Linden Assembly Plant is in a fight

for its future. In the 25 years I have worked there, we have overcome many threats to our existence. I am very proud of the Linden workers and what they have accomplished. But what we face now is by far the toughest yet. Adoption of the amendments we have proposed will help us win the fight to save GM Linden Plant and keep our workers employed well into the 21st century. But we need your help.

Thank you again, and we look forward to working with you on these important matters.

SENATOR LITTELL: Thank you, Mr. Noble.

Are you going to go next?

MICHAEL C. KARLOVICH: Yes, thank you very much.

Mr. Chairman, members of the Committee, and staff, I am Michael Karlovich, Director of Community Relations for Tosco Refining Company in Linden, New Jersey. Thank you very much for providing Tosco with an opportunity to testify today. We salute the leadership being shown by the Legislature, the Whitman administration, and the Board of Public Utilities in moving forward with the deregulation of New Jersey's electric utilities.

In our testimony, we will be addressing the changes proposed for the gross receipts and franchise taxes and related issues. First, we would like to provide you with some background on our company and our industry so that you have a clearer understanding of why lowering our cost of electricity is so critically important to us. Tosco moved into New Jersey in 1993 when we purchased the Bayway Refinery in Linden. Bayway has approximately 950 highly skilled employees who earn a combined payroll of \$63 million in 1996. Bayway produces more than 6 million gallons of gasoline every day, about

one-half of all the products we make. In fact, if our gasoline production were consumed solely in New Jersey, we would provide more than 1 of every 2 gallons sold in this State each day.

We also route flue gases from one of our processing units to a turbine to make approximately 200,000 kilowatts of electricity daily, which we consume internally. This power is currently tax exempt, and we respectfully request the Legislature ensure that self-generated electricity for on-site use remains untaxed under the GRFT reforms.

Our self-generating supply is not enough electricity to meet our own needs. In fact, we are Public Service Electric & Gas's single largest electric customer in this State other than government. Our total cost of electricity in 1996 was approximately \$41 million. This expenditure represents our third largest business cost after purchasing raw materials and paying salaries. We are currently purchasing power from PSE&G under a five-year flex-rate contract. The approval of this contract resulted in our foregoing an onsite cogeneration in 1993.

We are testifying today because we absolutely need to lower our electric rates so that we can effectively compete in our industry, which is a globally oriented and a commodity-based business. For example, New York Harbor is the destination for more than 50 percent of the gasoline being imported into the United States from foreign countries and as much as 20 percent of total Northeast demand is currently satisfied by these overseas imports.

The foreign refiners we compete against are primarily located in Europe, the Caribbean basin, Canada, and South America, as well as other

regions. These refineries, as well as most U.S. refiners, benefit from much lower electricity costs than ours. Consequently, lower utility costs and taxes are critical objectives for Tosco in New Jersey.

Unlike U.S. oil companies, many foreign refineries are either owned or subsidized by their governments. For example, PDVSA, the Venezuelan government's state oil company, is the principle owner of the number one gasoline retailer in the United States, Citgo. In addition, because Venezuela has extensive crude oil reserves, PDVSA is entering into crude oil processing agreements with numerous U.S. refiners against whom we compete.

The U.S. refineries that we compete with include the facilities in Texas and Louisiana where electric rates are sharply lower than Tosco pays in New Jersey. Closer to home, we compete with refineries in Pennsylvania and Delaware. Pennsylvania just deregulated its electric utilities, and we recently negotiated a very competitive rate with a large public utility for our refinery in Pennsylvania. So we have a proprietary basis with which to compare electric rates between the two states.

We are not alone. Sun, the largest refiner in the Philadelphia area, has also negotiated a competitive electric deal with a local utility there. All of the refiners that we've referenced view New Jersey and the Northeast as primary markets. To effectively compete with them and keep our jobs in New Jersey, we have to continuously find ways to lower our operating costs. This is largely because electric rates paid by our U.S. competitors generally range in the tenths of a penny on either side of three cents per kilowatt hour or lower versus the five to seven cents per kilowatt hour off-tariff rate we pay in New Jersey.

To illustrate how important electric costs are throughout our industry, refineries in states where electric costs are approximately 50 percent less than New Jersey's are still switching to cogeneration to further lower their rates. In an era of deregulation, lower electric rates are sensible means of lowering our operating costs, and there are a number of companies, including publicly traded utilities, that are willing to bid competitively for our business.

From a public policy perspective, lower utility rates should make it easier for the State of New Jersey to attract, retain, and expand business. This is especially important to the high-paying manufacturing sector where New Jersey has lost more than 300,000 jobs since 1975, according to the New Jersey Business and Industry Association. Many of these jobs were lost to states with lower operating costs than New Jersey's, including lower electric rates.

The erosion of New Jersey's competitiveness has been slowed by progressive measures championed by this Legislature. Nevertheless, the State's ability to attract, retain, and grow jobs is linked to utility prices. This is why reducing gross receipts and franchise taxes is only one component of the New Jersey Board of Public Utilities' vision for reducing utility costs in New Jersey, as referenced in the Board's electric industry restructuring plan.

Tosco agrees with this premise and encourages you to move forward expeditiously to reform the GRFT taxes while ensuring that self-generated electricity remains untaxed, as outlined earlier. Although Tosco is optimistic that New Jersey is heading in the right direction with respect to utility deregulation. We are particularly concerned about the proposed interim competition transition charge tariff, or our ICTC, which was outlined in a

petition to the New Jersey Board of Public Utilities by Public Service Electric & Gas on September 19, 1996.

We understand that Public Service desires to have the exit fee applied to its 2000 largest customers. Consequently, the State's largest electric users, including us, now find themselves in a frustrating position. They cannot negotiate electric contracts with another provider, and they cannot pursue new technology cogeneration investments. In summary, they cannot lower their electric costs or improve competitiveness. To our knowledge, the ICTC has not been endorsed as a means of recovering stranded costs by New Jersey's other electric utilities even though this issue is very important to them. Nevertheless, their largest customers also face the same uncertainty as we do.

Let me specifically explain why Tosco is concerned about this anticompetitive, antibusiness exit fee and how it directly affects our planning. According to the formula that PSE&G included in its proposal, if they were to develop a cogeneration option and leave the utilities grid, we would be required to pay an exit fee that would range from \$10 million to \$25 million per year for an indeterminate length of time.

This is a penalty that equals 25 percent to 50 percent of our current electric bill, which is unacceptable. From our perspective, exit fees provide the utility with a distinct negotiation advantage, not a means of recovering stranded costs. As we have stated, other utilities are retaining and developing competitive arrangements with their large customers without the need for an exit fee. In addition, the situation makes it very difficult to develop future business plans, particularly budgets. This exit fee proposal is

actually impacting our investment plans because of the uncertainties it has spawned.

As the rest of the State awaits competition and lower cost of electricity, is it appropriate to make the business environment in New Jersey even less competitive than it is today? In 1993, when we negotiated our off-tariff rate with PSE&G, competition was the key to PSE&G retaining Bayway as a customer. We asked: Why were competitive rates the desired remedy for retaining customers in 1993 but not in themselves a sufficient remedy in 1997? Why are exit fees appropriate at the onset of deregulation when for years large business customers have had the option to leave a utility without penalty? Why should the utility be allowed to discriminate against a select group of customers?

With these questions as a catalyst, we urge you, the members of this Committee and other interested legislators, to closely monitor the Board of Public Utilities actions with respect to exit fees. If this issue is not satisfactorily resolved via a BPU rejection of the proposal, we will return to request that you amend or pass legislation that would prohibit any utility from charging exit fees.

Quite frankly, New Jersey utilities should compete for customers rather than retaining them to exorbitant discriminatory exit fees. By becoming truly competitive, electricity suppliers and utilities will keep jobs in New Jersey, maintain shareholder value, and be a survivor in the brave new world of deregulation. Many utilities in other states are already acting in such a manner.

At a time when the State of New Jersey is considering ways to foster deregulation, we see the exit fee proposal as the antitheses of competition. The utility wants to compel us to remain their customer rather than competing with other suppliers for our business. When all is said and done, however, the State's best interest will be served by promoting competition not captivity.

To summarize Tosco's position:

- 1) Deregulation will be good for New Jersey's economy.
- 2) Proposed GRFT reforms are an important first step in lowering utility rates for all of New Jersey's energy consumers, as long as the reforms do not result in new taxes.
- 3) The anticompetitive, antibusiness exit fee proposal should be rejected.

That ends my testimony.

Mr. Chairman, thank you for providing Tosco with an opportunity to testify in favor of true deregulation of New Jersey utilities. At this time, I'd be glad to try and answer any questions that you or other members of the Committee may have.

SENATOR LITTELL: Okay.

Mr. Potter, did you want to say anything?

MR. POTTER: Yes, just a few brief comments, Mr. Chairman.

First, the Chairman of Local 595 of the United Auto Workers, Mr. Guy Messina, wanted to be here today and to demonstrate solidarity with the management of General Motors on their position. He could not be here. He's hopefully back there producing the highest quality trucks right now, but there

was some union work last night, and he could not be here today and extends his apologies for not being here.

I think it's important to note that GM and the union here in New Jersey are very much together on these positions. There have been some strikes in some other states but not at the GM Linden Plant where labor peace has been part of their formula for success for a long time.

We realize that we've interjected some new terms here today, departing load tariff by General Motors and for Tosco talking about this interim competition transition charge. It's the same thing, Mr. Chairman. It's a proposal filed by PSE&G last September that would charge a "departing customer" if they put in a cogeneration plant for the electricity. They no longer purchase from PSE&G, because they produce it themselves.

Assemblyman Bagger has said that he is going to sponsor an amendment to prohibit that. If you're talking about a level playing field in competition not, as Mr. Karlovich pointed out, captivity for customers, we need that amendment. In the case of GM Linden, however, just to reemphasize what Mr. Noble said, they need to build this cogeneration plant to have a thermal source of energy to replace the 61-year-old powerhouse.

There's nothing in this bill right now that benefits GM Linden. Right now if the bill is not amended appropriately and -- I know that the cosponsor, Senator Inverso, has been very committed and interested in coming up with the right formulation. Unless it's properly amended, it will be a tax increase.

Thank you, sir.

SENATOR LITTELL: Yes, sir.

If we put the amendment on similar to what Assemblyman Bagger talked to you about, saying that they couldn't charge you a withdrawal fee -- or whatever you want to call it--

MR. POTTER: That's a good term.

SENATOR LITTELL: --and if we allowed you to build your cogeneration replacement utility operation, would you be willing to do two things: After you've been able to capture the investment or most of the investment, come back on to a tax stream, and number two, would you give us some kind of indication that there's a long-term commitment for General Motors to stay in New Jersey, and also for Tosco?

MR. NOBLE: Well, with regard to General Motors, on the first issue we compete on a domestically and foreign competition, and we look at the energy cost in other states. Right now, the tax issue where the imposition of additional taxation on gas that we purchase today would put us at a disadvantage with other plants that we compete with today, both in this country and abroad. So we see that as a disadvantage going forth. Obviously, things change in other states, too, but at this point in time, we see it as a disadvantage for the New Jersey operation and a distinct disadvantage with other states, mainly in our case, for example, Louisiana and Ohio.

With regard to long-term outlook for continued operations in New Jersey, that particular decision is made on a lot of various issues including availability of a product line, timing, the workforce, cost of doing business in the State-- All those things we are working very hard on, but at this point in time, there is no guarantees. We have actually even looked at the cost of-- What would it cost to close down the operation even with the cogeneration

plant. But, unfortunately, without a cogeneration plant, there is no future. The plant will not be given a new product. With the cogeneration plant, we at least have a fighting chance, and our workforce back in Linden is working very hard on a number of different fronts to improve our operation to make it real hard for General Motors to close that plant down.

SENATOR LITTELL: Do you use total quality management operation?

MR. NOBLE: That is one of the many things we are using to get there.

SENATOR LITTELL: How's your production off that line compared to other competing facilities?

MR. NOBLE: We have recently and in the past couple years increased our line speed twice. We are the export plant for this particular product line and also the flex plants so that we float with the market. Right now we are in the process where we'll be introducing right-hand drive vehicles for export to Japan and next year -- which is the first truck products that will be so designed for exporting to the foreign markets. We're doing anything we can to put our best foot forward as a plant and, also, obviously for the benefit of General Motors. If you need to do it everyday and you're only as good as the last time you've been graded -- so we are working hard to make sure we're always in the spotlight and doing the right things.

SENATOR LITTELL: What about Tosco? What's your view on giving you some kind of an incentive to do your cogeneration and recapture your investment over a period of time and then come back on and pay taxes? Does that seem fair to you?

MR. KARLOVICH: Mr. Chairman, with all due respect, our situation is similar in many respects to what Mr. Noble just outlined for GM. However, we are new to the State. We purchased the Bayway Refinery from Exxon. At the time, Exxon was looking at the possible closure or turning it into a products terminal and selling it. We came along and purchased it with a long-range view of the facility. We have been investing in the refinery which had not be done for approximately, in terms of major capital improvements, for 13 years prior to Exxon selling the facility. We have been investing in the plant in a number of ways. We had Governor Whitman in for a ground breaking on a \$48 million project two years ago that has since come on-line. We've made numerous improvements and enhancements to the plant.

Quite frankly, rather than return to the tax roles, we would prefer to see investments in the plan, many of which are in fact mandated by government. We are not able to go to the government and look for subsidies on the investments that we need to make clean fuels, such as reformatted gasoline, which has lead to cleaner air in New Jersey.

We have to look at the entire package. We have not stated that we are ready to go with cogeneration, but we think we need that as an option. In 1993, we bypassed cogeneration because Public Service was able to come up with a competitive rate. So we went with it. That could happen again. At the time, they made the petition for ICTC, or exit fee. We were in active negotiations with them, as well as some other providers of electricity.

We're not saying that we want to go-- We're not saying that that's our option we're going with. We're still looking and talking. Well, we had been talking with Public Service at that time. Since then--

SENATOR LITTELL: Do you want it to be an option?

MR. KARLOVICH: Sorry?

SENATOR LITTELL: Do you want it to be an option?

MR. KARLOVICH: Yes, we would actively pursue it if it's similar possibly to the rates that we got in Pennsylvania. We think the similarities between the utilities in Pennsylvania and New Jersey are apparent. Once this exit fee issue is cleared up, possibly by the BPU, we may go back into discussion with Public Service again.

So again, there are many aspects to the issue. But our intention is the long-term commitment to New Jersey. It's very difficult today to pick up a refinery and move it, and quite frankly to permit a new refinery in any state would be difficult.

MR. POTTER: Senator, if I might also comment for General Motors, the concept of phasing out the exemption based upon the speed at which the capital investment is recaptured, I think, has a lot of attractiveness to it. It's a very interesting concept. We haven't yet had a chance to consider that as a possible refinement to the legislation. We certainly would like a chance to do so and to get back to you and other members of the Committee and, of course, Senator Inverso and Senator DiFrancesco as the cosponsors. I think we could foresee some accounting difficulties. I'm not one to talk about accounting difficulties to someone like Senator Inverso, but nonetheless, we think that might be a feasible way to do it. But we don't want to commit here on the spot until we've talked to the others who are involved in developing this project, which has really been in gestation now for several

years. It has now been sort of clipped off at the heels, so to speak, by this tariff, or exit fee, that was proposed by PSE&G.

I might point out, if I could, that General Motors has filed a motion at the Board of Public Utilities to try to get an early ruling on the situation. I used the word early somewhat advisedly since this has been pending since September 1996. General Motors filed a motion on October 6, 1996 seeking an early decision on it. Tosco filed a similar motion October 15, also, seeking the same relief. We've been extremely frustrated frankly by the situation. And now General Motors is trying to-- Rather Quixx, the partner of General Motors, is trying to go to closure on financing of this, really a small cogent project, 25 megawatts, but they have been told in no uncertain terms by the bankers and investors in other groups that they will not commit to this project as long as this cloud is hanging over it, this departing load tariff.

We have scheduled a ground breaking for the project for mid-June 1997. We have had very encouraging signals from the DEP. This project is going to reduce pollution in Linden significantly by going to this cogeneration plant, but everything is on hold, and yet, GM has got to have a powerhouse in operation by the winter of 1998-1999. It's really an imperative and an almost desperate situation right now. So we look forward to working with you, and we seek your help.

SENATOR LITTELL: Thank you, sir.

Let me turn it over to my Vice-Chairman, Senator Inverso, and the cosponsor of the legislation.

SENATOR INVERSO: This exit tax assessment-- While it does seem very egregious, there's nothing in any agreement you've had with Public

Service that would provide them this opportunity to impose the tax without getting authorization from the Board of Public Utilities Commission. This is a whole new concept.

MR. NOBLE: Yes, that's correct.

SENATOR INVERSO: You're on.

MR. POTTER: Okay. Sorry.

That's correct, Senator. We went through a year and about a 16-month review of the project at the BPU, starting in, I guess, the summer of 1995, to review the entire General Motors project. PSE&G opposed it along the way, and one of the things they said in this was, "Well, we're going to want to charge you some kind of exit fee." We immediately, in an interrogatory, said, "Well, give us the basis for it. What is going to be stranded? What facilities have you committed to General Motors that hasn't been paid for over and over again several times?" and they declined to answer those questions.

It was only after the BPU issued a declaratory ruling approving the project, I think, six weeks later that they filed this departing load tariff thing, which really is sort of a Damocles over the project.

SENATOR INVERSO: Sure. You mentioned in your testimony \$3 million. You didn't say how many years. What is the aggregate amount they're after?

MR. NOBLE: Right now, from what we can read into it, it may be indefinitely. It's really absurd when I go out of business and leave the State and it doesn't cost anything, but I put a cogeneration plant in, I have to pay \$3 million a year for something I'm not buying. I wish I could get the kid a

deal that if you buy a Ford, you'd pay me for the Chevy, but it doesn't work that way in the market.

SENATOR INVERSO: Is there anyone here from the BPU? Mr. Tate was here, I guess he left. Well, we'll inquire as to why this thing isn't being expeditiously resolved. It does seem to me on the surface, from what you tell me, to be very egregious, and that's the kind of thing--

SENATOR KYRILLOS: It's not part of this bill, though, is it?

SENATOR INVERSO: No. I was going to say, it's not part of this bill. This is the other thought I had. Assemblyman Bagger has indicated his intent to put an amendment into this bill to deal with that issue. I mean, while on the surface it's not part of this bill, it seems to me to be part of the whole deregulation of the industry. But that may be too late for you.

MR. NOBLE: Right. That's correct.

SENATOR INVERSO: You need to deal with this at this point in time, and the best we can do, short of putting it into legislation, which we may have to do, is to make sure the BPU knows our concern about the urgency of resolving this issue for you. Because, clearly, you can't make a rational capital decision with this out there. As you say, it's a Damocles sword hanging over your head, as well as Tyco's head.

I'd love to hear someone from Public Service at some point later on this afternoon tell us why this tariff is filed. Because we know we have to recognize stranded cost, that we have to deal with this issue. This bill does not deal with stranded cost, but at some point when the legislation for the entire deregulation has to be acted upon, the stranded investment cost has to be dealt with. This looks like it's somewhat of an early attempt on their part to deal

with this issue apart and beyond from it being dealt with globally, in terms of whether we're going to securitization or some other approach to dealing with that stranded cost.

I'm glad you raised the issue because, you know, we keep it on our antenna, and I'll be glad to reach out to BPU for you to see if I can get them to move this thing forward. If there's no resolution there judiciously, then we'll take whatever other step may be necessary to help you. We need to help you.

We wish you had-- The question about the processed gas. You're now buying it in an unbundled fashion.

MR. NOBLE: That's correct. We've been buying for approximately 10 years.

SENATOR INVERSO: Right. Okay. So you will be part of that 5-year phase back which, I guess, is not really palatable to you, but--

MR. NOBLE: No, in fact, even with the 5-year averaging, because part of that time frame our plant was down for model change conversion, it's going to be hard-- We going to be hard pressed to even have a decent average to work from for the years that were grandfathered.

SENATOR INVERSO: Right. Well, if we could-- I don't know if we could take care of all that you ask for. I think we're sympathetic. Certainly we want to see General Motors stay in New Jersey, not that you've threatened to leave. On the other hand, I didn't hear you make a guarantee that you wouldn't leave. And here in West Trenton, of course, we know the situation there. It seems to me if we can help you with the exit fee, if you will, if we can help you with your cogeneration facility, time that with your

recoupment of your investment, as Senator Littell suggested, I think that's a sound suggestion. That may go a long way -- a long way -- to giving you what you've asked for, for our consideration. And if we can help you on all four points, fine, but those two seem the most possible in my opinion.

MR. NOBLE: We appreciate any help you can provide us, Senator.

SENATOR INVERSO: Thank you.

MR. POTTER: Thank you very much.

MR. KARLOVICH: Thank you.

SENATOR INVERSO: The next speaker is Gary Epler, the Managing Attorney for Electric and Gas, the Division of the Ratepayer Advocate.

GARY EPLER, ESQ.: Thank you very much, Mr. Chairman, members of the Committee. My name is Gary Epler. I'm the Managing Attorney for Electric and Gas for the Division of Ratepayer Advocate. I'm appearing today on behalf of Blossom Peretz, Ratepayer Advocate. She sends her regrets to the Committee. She had a previous commitment and is unable to appear today.

We have distributed prepared remarks to the Committee, and in the interest of time, I will not read that into the record but attempt to summarize our position on this matter.

As you may know, the Division of Ratepayer Advocate represents the interests of utility consumers in the State of New Jersey including the interests of industrial small-business and residential customers. The Ratepayer Advocate supports the bill for the most part before you, and we applaud the efforts of the various parties that went into the crafting this bill and feel that

there are benefits generally for all ratepayers. There are, however, several changes to the legislation that we believe would provide additional benefits and protections for ratepayers and taxpayers, if I could briefly describe those.

The first suggested change is to consider an ad valorem tax on utility-owned transmission plant within the State. We see this as a possible additional source of revenue in case there is a shortfall from the transition portion of the tax. The benefit of such an ad valorem tax is that out-of-state suppliers and users of utility-owned transmission systems located in our State would bear a portion of these costs proportionate to their use of the system. That's precisely the situation now with New Jersey suppliers and users who bear a portion of the property taxes on transmission lines, which they use in other states.

The second issue that we believe would be an appropriate amendment is perhaps more controversial, and that concerns the tax benefits to independent power producers, or IPPs, that are proposed under this legislation. Basically, as we understand the proposed legislation, it not only exempts the sales of electric power by IPPs for resale, but it exempts from the sales and use tax purchases and delivery of natural gas to IPPs. What we are concerned about is that the exemption is offered to the IPP industry at a time when New Jersey ratepayers are being asked to absorb billions of dollars in uneconomic costs associated with certain long-term purchase power agreements which the utilities entered into with these same IPPs.

The Board of Public Utilities, in its report that was referred to by Board President Tate earlier, was issued on April 30, 1997 to the Legislature and to the Governor, recognized the burden that these contracts have on

ratepayers and recognize its own inability to compel the renegotiation of these contracts directly and has specifically requested the Legislature's assistance. As discussed in detail in the Board's report, and here I quote from the Board's report, "Without submitigation of high-priced IPP contracts, it will be much more difficult to achieve any near-term rate reductions." High-priced, nonutility generators' contracts contribute in no small way to the current high level of rates experienced in New Jersey. Indeed, the status report estimates -- attributes anywhere from one-third to one-half of the entire straight-across problem in the State to above market IPP contracts. Moreover, these contracts are primarily long-term agreements, mostly 20 years and in some cases up to 30 years, with many years remaining. To date, with some limited exceptions, there have been very little evidence of attempts on the parts of IPPs to volunteer in negotiations to mitigate the relatively high prices being paid by utilities under these contracts.

Accordingly, the Ratepayer Advocate proposes that the legislation make the eligibility of an IPP holding above market power purchase contract agreements with New Jersey utilities for tax exemptions and natural gas purchases contingent on a finding by the Board of Public Utilities that the IPP has made a good faith effort to renegotiate these agreements.

The third proposed area that we would suggest an amendment has to do with the elimination of what we believe is a punitive disincentive for municipal utilities to expand their service territories. Again, as we understand, the current legislation that's proposed here is that the municipal utility which expands beyond its current service territory would be subject to the sales and use corporate business tax not only with respect to the revenues and net

income from these additional sales, but lose its existing exemption from sales and use and corporate business tax with respect to all operation, including those within its historic service territory.

Accordingly, we propose that municipal utilities which choose to expand outside their traditional service territory retain existing tax benefits with respect to operations within their existing service territory, in other words, be grandfathered for existing operations and lose only their exemption with respect to new business outside their historic service territory.

The fourth and final subject that we believe would warrant an appropriate amendment is creating a positive tax for municipal aggregation. As you know or may be aware, under the Board's proposal, the competitive choices will be available for all classes of customers. We have a particular concern in our office that there are certain advantages due to load shape and load characteristics that industrial and commercial customers may have in terms of being served by alternative suppliers.

We believe that the best way to ensure that small customers, residential and small commercial customers, can be served in a competitive environment would be to encourage municipal aggregation, and we see that there is an opportunity to do this under this legislation, and that is to allow an exemption for municipalities' own use, not for the use of its constituents, but for its own use, if the municipality aggregates its customers. That's basically an additional exemption that we pose. We feel that this would help encourage municipalities to take on the task of aggregation.

With that, that concludes my comments. The details of these proposals are laid out more specifically in the prepared remarks. I'm also available for any questions.

SENATOR INVERSO: Thank you.

When we met, you presented these points with the Ratepayer Advocate, and I believe there's some very good points. I think they do require and warrant, I believe, deliberation. I will take up with the Senate President, who's a close sponsor of the bill, and discuss them further.

The municipal aggregation, I think, makes sense. I think it's a way to help the residential consumer in this array of choice that's going to be confronting them. I do like the concept, at least of the IPPs, sitting down and seeing if we can resolve some of these high-priced contracts that the utilities are locked into with them. I don't know whether we need to have the stick to do this, but certainly it would seem to make sense. And as you say, that would go probably a long way in helping with the -- lowering the level of the stranded costs that we have to deal with.

Do you know how-- You mentioned New York and Niagara Mohawk, I believe. Do you know how it was they sat down? Was it--

MR. EPLER: I don't have specifics exactly, but I think it was probably a combination, as they say, of the stick and some incentives. I think that's entirely appropriate. I think we need to be creative to think of some incentives also in addition to this kind of approach.

SENATOR INVERSO: If you could find out for us what the catalyst was between the IPPs and Niagara Mohawk that the State of New York utilized.

MR. EPLER: My understanding is that there were very various things going on. I think that the chair of the commission was directed by the governor to get personally involved. I think that's one effort that was undertaken. I think that Niagara Mohawk took a very hard-line position. My understanding is that there was some discussion of possible bankruptcy and the ramifications that that would have on these contracts. I think also we speak of incentives. I think that Niagara Mohawk was able to sit down with these various entities that it had the contracts with and able to show that really it was in their own best interest to come up with the result that they did, but there were certainly economic considerations of serving that particular territory in that all would benefit in coming up with some kind of compromise.

I think that probably we can get to the same place here within this State, and I think it requires certain leadership from the Board and from the Legislature directing parties to get together. We certainly volunteer our office to participate and help in that regard and, as I said earlier, to try to be creative in some of the incentives that we could propose to enable the parties to the contract to still try to realize the benefits that they entered into and that they hope to achieve initially.

SENATOR INVERSO: Any questions or comments?

Thank you very much.

MR. EPLER: Thank you.

SENATOR INVERSO: The next speaker will be Mayor Millard Wilkinson, Lou Neely, and Jon Moran, New Jersey League of Municipalities. Jorge Rod, Administrator, Lacey Township.

MAYOR MILLARD WILKINSON: Good afternoon, Vice-Chairman Inverso, and members of the Committee. I'm Millard Wilkinson, Mayor of Berlin Borough and also the First Vice-President of the New Jersey League of Municipalities. For the past two years, I have served on the League of Municipalities' Utility Tax Reform Committee. For even longer than that, the League has been warning State-level policy makers of the need for reform. We are extremely pleased that the Legislature is prepared to resolve this issue.

In order to understand our position on S-31, I will need to talk a little bit about its companion bill, S-30. And while we realize that S-30 is not before you today, you must all realize that the two bills must move together and must both be enacted if utility tax reform is truly to benefit the people and the businesses of our Garden State.

First, let me say that we committed to timely action on the legislation. Our position was forged on a bipartisan basis. This issue is too important to municipal officials and to the property taxpayers who they struggle to serve to be used to serve partisan political ends.

The fact is that the gross receipts and franchise taxes can no longer deliver the reliable property tax relief punch as they have in the past. From 1995 to 1996, New Jersey municipalities lost \$52 million from this source. But for the severity of the winter of 1995 and 1996, those losses would have continued into this year.

The tax policy changes contained in S-31 will help to solve this crisis. This is a good bill. With just a few amendments, we will be happy to give it our unqualified support and to join in the push for its passage. We have

given the Committee full explanation of the need for these amendments, and I will at this time give you a brief summary.

First, we need explicit legislative recognition of the right of municipalities to continue to enforce existing and to negotiate future host community benefit contracts for energy and telecommunications facilities within their jurisdictions. Because of the elimination of gross receipts and franchise taxes and because of the other parts of our State's tax policy, host community benefits are needed to protect our residential property taxes.

Second, language that should subject municipal electric utilities to the sales tax and the corporation business tax, if they decide to expand their service areas within their municipal boundaries, needs to be removed. As a practical point, this would penalize one municipality, the City of Vineland, and it benefits only one investor-owned utility, Atlantic Electric. The ability of Vineland Electric to extend service throughout the municipality is a vital part of the city's economic development strategy. That strategy should not be undermined by the provisions of S-31.

Third, certain language in the bill could be read to penalize any municipal electric utility that sites any new installations even within its current service area. We are certain that this is not the sponsors' intent, and we urge you to clarify this language.

Fourth, the bill contains language which would exempt future telecommunications service providers from the same local personal property tax currently paid by Bell Atlantic and others. In the interest of equity and fair competition, we urge this Legislature to permit the imposition of the same tax on all new entrants into the competition for local exchange service market.

We have one observation on S-31, and this is not a request for amendment. S-31 would for the first time subject public sector purchasers of goods and services to the State's sales and use tax. While we recognize the need for this provision and appreciate the fact that we will enjoy a substantial net revenue benefit because of it, we still see this as a dangerous precedent.

All involved in the process must realize the unique set of circumstances which dictates our support for this provision in the context of utility tax reform. Likewise, all involved must realize that any attempt to extend this precedent will meet with our strenuous resistance.

With regards to S-30, the Energy Tax Receipts Property Tax Relief Act, we urge you all to keep these facts in mind:

- 1) Public utility gross receipts and franchise taxes are designated to compensate municipalities for the use of the public's rights-of-way and for the services provided by municipalities to utility facilities.

- 2) The State, at the request of the utilities, has standardized the tax rate and made itself the collection agent for these taxes.

- 3) The distribution of the proceeds to municipalities is not State aid. Rather, it is the conveyance to municipalities of revenues to which they are statutorily and constitutionally entitled.

Implicit in S-30 is a State-level acknowledgment of those facts. We sincerely appreciate that the poison pill provision is testimony to the lengths you will go to protect our property taxpayers with a basic level of the new utility tax revenues. And it is to the sponsors' credit that we have included such novel and reliable protection. S-30 needs only a few modifications to earn our unqualified support. Again, the Committee has been

provided with a full description of those changes. I will only highlight their purposes.

The amendments we seek are designed to:

1) maximize the property tax relief potential of the Energy Tax Receipts Property Tax Relief Act by increasing the amount to be distributed in the first year to the amount distributed pursuant to its predecessor taxes, during 1995, the year during which our property taxpayers enjoyed the greatest benefit from those taxes;

2) promote predictability by providing a formula for the full distribution of energy and telecommunications tax revenues;

3) provide for the incremental increases to the fund in order to insulate our property taxpayers from the effects of inflation on the ability of this revenue source to restrain future tax increases;

4) prevent prospective State skims of the revenues derived from the utility taxes, which were designed to compensate our citizens for the privilege granted to the utilities to use the public's rights-of-way in order to secure private profits.

I thank you for your time and your kind consideration. I look forward to working with you all and with the sponsors so that our property taxpayers, as well as our utility ratepayers, can enjoy the benefits of utility tax reform next year. After all, they are all of the same people.

A couple of my colleagues have comments that they would like to make at this time.

L. MASON NEELY: Thank you, Senator Inverso, and thank you for establishing a record.

I want to just reiterate a couple of things and make a comment on what may seem to me be somewhat disingenuous on the part of one of predecessor speakers. First of all, the League is taking this not as the Republicans, the Democrats, or the Independents. We've taken this as nonpartisan. We support this. We'd like to see the legislation happen. We'd like to see it happen fast. We think it can happen before July 1. So our time line is to move it and work with you as quickly as we can.

Secondly, there was some discussion earlier about the date of March 10, 1996. The bill has March 10, 1997. My understanding is there are three companies that have applied for the air quality permit. GM is one of them, and they would have the exemption. And for them to come up and testify as if they are under dire straits because of that -- they're rolled in. They are the one who have applied for the air quality permit before that. And I think their comments may have been somewhat skewed to create a crisis that really doesn't exist. I think we need to recognize that. You should have from DEP who the three are that have applied for the permit, because GM is protected under the grandfathering act.

Number 2, under Section 60, line 20, we do not want to see that date of April 1, 1997 in there. We think the future of telecommunication industry is going to be important, and we want to reiterate that that date should be taken out.

Parallel with that, you're going to hear AT&T come in and say under Section 69 that the date of January 1, 1998 should be taken out. We think that date should apply, because anyone who is not paying the tax now-- We don't know what the future is going to be. There is no tax incident, but

that certainly is something that does protect municipalities, and we think Section 69 should stand as you've drafted it and it is written.

To that extent, we know that the cogeneration, the IPPs, have made significant revenues at the expense of the sheltering it from gross receipts and franchise tax. We think it is time, as Senator Littell has suggested, that they be phased back in, that everyone be on a level playing board. We very much support that phasing in. That's part of your bill, and we think that should be part of it. It's going to be important to the revenues, as you phase out TEFA, that you bring other people back in; and as you make it a uniform tax, giving someone a shelter from a tax -- it was a local government tax -- is not good business. It simply means that everyone should compete on an honest level, and we support very much that concept.

With that and the other couple of amendments we've made, we do support this legislation. The League has spent a long time-- We've testified over the years that this revenue is bleeding, that changes need to be made, and we endorse and support you.

Thank you very much for your willingness to work with us, and this bill is a good bill.

J O R G E A. R O D: Mr. Chairman, I'm the Administrator from Lacey Township, former legislator, former mayor, former councilman in my town of Lacey Township. I have a two-page statement, and I would just give you a copy, and I'm just going to summarize my two-page statement.

Just so you know, the gross receipts and franchise taxes revenue is going to diminish at a very fast rate. So, as Lou Neely and my colleagues stated to you, this legislation has got to be put in place as soon as possible to

stop the erosion. I think this is a good piece of legislation, and the mayor and the township committee, which are my bosses, are in favor of this bill and would like to see this done as soon as possible.

Thank you. I have a two-page statement, Senator Littell.

SENATOR LITTELL: Thank you.

Senator Inverso. Senator Inverso, do you have any--

SENATOR INVERSO: No.

SENATOR LITTELL: --comments or questions?

SENATOR INVERSO: No. I do want to commend the League for working with us on this issue. As was said, this is purely a nonpartisan or a partisan-- This is a public issue and partisanship never played a role in this. That's important in terms of support we've gotten from the League in this issue. Thank you.

MAYOR WILKINSON: Well, thank you. We appreciate that very much. No question it's nonpartisan. It becomes more an economic issue than anything else at this point in time.

Thank you.

SENATOR LITTELL: Thank you, Mayor.

Senator Ewing and Senator Kyrillos, you didn't have any questions?

SENATOR EWING: No, I didn't. No, sir.

SENATOR LITTELL: Thank you.

Marlene Asselta, South Jersey Development Council. She here?
(no response)

Jeffrey Lucas, Cherry Hill Economic Development Corporation,
is he here? (no response)

Richard Fritzky, Meadowlands Regional Chamber of Commerce.
Do you have copies of your testimony for us?

RICHARD FRITZKY: Yes, I do.

Senator, I'll be very brief, and thank you for the opportunity. I'm
not going to read--

SENATOR LITTELL: Push the button and speak into the mike,
Rich.

MR. FRITZKY: This one right here? Do you have me now?

SENATOR LITTELL: Yes.

MR. FRITZKY: Senator, thank you for the opportunity. I do
have a very short statement. As eloquent as it might be, I'm going to forgo
that. Although I'm here on behalf of the Meadowlands Regional Chamber of
Commerce, I'm a constituent of yours, and I value your good time.

Simply put, I took the time out this afternoon to come because we
believe this is very important legislation. It's long overdue. We're facing great
changes given the deregulation that's to come in the marketplace. Frankly we
don't believe we've even begun to ask 90 percent of the questions that we will
be asking, but this legislation in the aggregate, in the gut, and in the heart is
good. It makes sense. We know nothing is perfect. It's going to be tweaked.
We're going to find that there are nuisances and factors and components that
have to be considered as we go forward, but the world is changing. This
legislation, in light of that change, makes great sense. We urge you to move
forward with it.

I'll leave copies of my brief statement with the Committee.

Thank you.

SENATOR LITTELL: Thank you very much.

Does this affect your ability to be competitive in that metropolitan region?

MR. FRITZKY: I don't think there's any question. I think in the heart of what we're talking largely today about -- level playing fields and balance and fairness and equity, and everyone coming forward to, as we go forward, pay their fair share in the energy retail marketplace-- In the heart, this is an economic bill. This is an economic investment bill. This is a bill about New Jersey, about dollars, about the generation of jobs going forward. It makes sense.

SENATOR LITTELL: Thank you very much.

Any other questions from the members? (no response)

Thank you, Richard. It's good to see you.

Next is Steven Montovano, Enron Corporation.

Push that button so the red light's on, please. (referring to microphone)

STEVEN MONTOVANO: Thank you, Mr. Chairman.

I'd like to start by applauding the efforts of your Committee and Assemblyman Bagger and his efforts on his Committee and offer support for most of the proposed legislation as it concerns the energy tax laws.

Enron believes that the equalization of taxes is needed and it's correct to do so. We have one area of concern which I'm here to talk to you

about. It goes in line with the “levelizing” of the playing field that you’ve heard so much about today.

I want to talk a little bit about how the gas is bought and sold at the utility level and compare the utility customer who buys his gas from the utility to the nonutility customer who buys his gas from companies like Enron. They basically pay three components when they do that. The utility customer pays the utility for its gas, as the nonutility customer would pay Enron for its gas. The utility customer pays the gross receipts and franchise tax that, as we all know who are here today and have been following this issue, is more when they buy their gas from the utility. They pay a higher gross receipts tax to the utility. The nonutility customer pays a lower tax to the utility when he buys his gas from a company like Enron.

It’s the third component that I’m here to talk to you about, and it’s the component that each customer pays the utility just to distribute the gas and bring it to its establishment. The utility customer pays a much lower rate to do this, and the tax and equity that we’re here to talk about isn’t going to levelize the playing field. That’s the component that’s keeping the playing field level. By having that tax and equity in the utility rates, the nonutility customer is paying more right now to have the utility to deliver Enron’s gas. Enron and companies like Enron are providing services to that customer and selling that customer gas that the utility no longer provides. It’s companies like Enron that manage the gas for that customer and deliver the gas to the distribution system to the utility.

The utility is still charging our customers for these services that we are now providing. This is the inequity that our proposed amendment looks

to address-- I'm not reading from my comments today. I'm trying to paraphrase them, as you can read them later. In essence of time, in having everyone come up, I thought it would be quicker just to go through the highlights.

This inequity in the rate side is what our proposed amendment looks to address by asking you to mandate to the BPU that before any change goes into effect on the natural gas side -- and it's important to note that we're not here to try to change this bill moving forward on the electric side. The electric competitive market is not opened yet. There is no rate in equity in the electric side. The inequities are on the gas side where the markets are already open.

Our amendment asks you to mandate that the BPU, before initiating any changes on the tax side, review and fully review and implement the proper distribution rates, so nonutility customers, as well as utility customers, pay for the services they utilize.

The chart and the attachment to my testimony clearly shows that in the first year after passage of this bill, nonutility customers who are now buying gas from companies like Enron will clearly see a significant increase in the amount they pay for their natural gas needs. And even at the end of year five or the end of the TEFA adjustment, they'll continue to pay more. Over the five years, for this one customer who uses an equivalent amount of gas to the local pizzeria will pay over \$3500 in additional taxes included in their gas bill.

The solution to this problem is to amend your bill with Enron's amendment and have the BPU adjust the distribution rates that these

customers are now paying the LDCs, the utilities in this State, to reflect only the services that the utilities are providing.

At this time, I'd like to entertain any questions you may have.

SENATOR LITTELL: Senator Inverso, do you want to comment on this first?

SENATOR INVERSO: Well, let me ask-- This chart here (indicating) depicts what the -- in this case, what this consumer would be paying after the five-year phaseout.

MR. MONTOVANO: Yes. What I tried to reflect in my chart is the usage of, say, a pizza parlor in the State of New Jersey and the base share that they would be paying today before the tax change.

SENATOR INVERSO: What they're paying, let's say, to a supplier like Enron?

MR. MONTOVANO: Supplier like Enron-- And that includes--

SENATOR INVERSO: In addition with the transportation costs included?

MR. MONTOVANO: Excuse me?

SENATOR INVERSO: The transportation costs are included in there?

MR. MONTOVANO: Transportation, as well as gas, as well as the existing taxes.

SENATOR INVERSO: Right.

MR. MONTOVANO: So with the tax increase to that customer in the first year, it equates to about \$900.

SENATOR INVERSO: That's the 6 percent sales tax--

MR. MONTOVANO: Well, if--

SENATOR INVERSO: --and TEFA?

MR. MONTOVANO: What I've done in my analysis is that--
Assume that customers no longer pay the gross receipts tax--

SENATOR INVERSO: Right.

MR. MONTOVANO: --and they moved to pay the sales tax, the corporate income tax, as well as the TEFA. The TEFA is what brings the rate down over the five years.

SENATOR INVERSO: Right. That's the phaseout.

MR. MONTOVANO: But as you see at the end of the five years, the customer is still paying \$600 more. Now, the important point to make here-- That customer is not going to pay \$900 in the first year. That customer is going to go back to the utilities. There's not \$900 available for that customer to make up that shortfall. He's going to leave the competitive marketplace, and he's going to go back to the utility, and competition will go away.

SENATOR INVERSO: Question: Why would he go back to the utility? Let's presume that the \$10,383 is a favorite price. The customer's gone shopping. This is a good price.

MR. MONTOVANO: Right.

SENATOR INVERSO: The next year, when this legislation is in effect, it roughly goes up by 9 percent -- is what you're projecting here.

MR. MONTOVANO: Rough numbers.

SENATOR INVERSO: That's still on the base of a favorable price.

MR. MONTOVANO: No, it's not.

SENATOR INVERSO: Are you saying the utilities will now come down to meet your price?

MR. MONTOVANO: You've got to remember what the utility price will be-- Will be something equal to the existing sales rate that the base share price of \$10,000, which is competitive against the utility price under the existing tax structure--

SENATOR INVERSO: The 13 percent?

MR. MONTOVANO: Right. When you take just part of the tax structure away, that customer will now have to continue to pay distribution rates to the utility that are higher than if he just goes back to be a sales customer. He will pay something greater than the \$10,383. He will still see an increase, because he's going to go back to the utility, but it will be less than the \$900 increase that it would take for him to stay with companies like Enron.

SENATOR INVERSO: The differential in the cost here for the base year is the gross receipts and franchise tax equivalent of about 13 percent. Is that what you are saying? That's why this 10,383 is the number it is. It says it doesn't include that--

MR. MONTOVANO: The 10,383 includes the reduced gross receipts and franchise tax, but it also includes the higher distribution charge that the company's paying.

SENATOR INVERSO: Okay. Well, okay, but there is a distribution charge that's loaded into the cost by the utility?

MR. MONTOVANO: Yes.

SENATOR INVERSO: And it's at a price that you charge the customer, in essence?

MR. MONTOVANO: Well, the distribution charge is the charge that the utility charges the customer.

SENATOR INVERSO: Right.

MR. MONTOVANO: Enron would charge that customer to manage its gas supply and provide the gas supply to that customer.

SENATOR INVERSO: Right. Okay. All right. So in the year two, if nothing happens, the customer stays -- has Enron manage -- I'm talking about after the year one, the first year after the base share, year one-- The only thing that is going to happen is that there will be now, in your estimation, a 9 percent add-on cost. Is that right?

MR. MONTOVANO: Rough, yes.

SENATOR INVERSO: The cost will go up 9 percent. The consumer, the customer, always has the option of where to go, but you're saying that this 9 percent is so pejorative that the customer will go back to the utilities?

MR. MONTOVANO: Right because, Senator, you could figure the utility price is somewhere between the 10,383 and the 11,312 because of that difference in the amount that the utility charges to distribute the gas.

SENATOR INVERSO: You're saying it's all in the distribution component. I've never--

MR. MONTOVANO: Yes, and that's the importance of our amendment is to have the BPU look at that difference and adjust that difference before a tax change goes into effect.

SENATOR INVERSO: All right. At the end of year five -- in the year five, the 10,943, you're saying it's about roughly \$600--

MR. MONTOVANO: Yes.

SENATOR INVERSO: --greater because of the distribution charges again? That's the differential?

MR. MONTOVANO: But again, you have by year five-- You have the customer who's currently paying a tax of about 16 cents, at the end of year five, will be paying a tax of roughly 36 cents, the equivalent of whatever the gross receipts tax, the energy tax. On the top of that, he'll still be paying more to the utility to distribute his gas.

SENATOR INVERSO: Well, he'll be paying for distribution. The gas has to get to the customer. You can't--

MR. MONTOVANO: Right. But when he buys his gas from the utility, he pays the utility less to distribute the gas than what he pays Enron to distribute the gas.

SENATOR INVERSO: All right. So what you're saying basically is that the utilities are allocating, or loading, more costs into the distribution when it's a customer off their system than it is when it's a customer in their system. Is that what you are saying they're doing?

MR. MONTOVANO: Yes, what I'm--

SENATOR INVERSO: And essentially--

MR. MONTOVANO: Essentially, what I'm saying is, when Enron provides gas for the customer, they're also providing not only the gas, but management services to manage that customer's gas supply.

SENATOR INVERSO: So this is really a cost accounting tariff--

MR. MONTOVANO: It's a cost allocation issue.

SENATOR INVERSO: --issue, the tariff that the BPU should take a look at.

MR. MONTOVANO: And that's what our amendment looks to do, is have the BPU address this issue, because--

SENATOR INVERSO: Have you found this to be true in other states that you're dealing in?

MR. MONTOVANO: Well, it's--

SENATOR INVERSO: Let's say California and Pennsylvania. They're a little bit ahead of us, maybe a step or two ahead of us. Is this happening there?

MR. MONTOVANO: It's not as significant in other states. The number one reason is the tax itself is not 13.5 percent. In other states, the transportation rates, or the competitive market rates, that were designed were designed without recognition of any tax inequities that may have existed. The tax playing field was already leveled, if you would, when they went to adjust the utility rates to offer competitive services.

The problem in New Jersey was, in the development of these rates, the tax inequity was built into the "competitive" rate. So all it did was mask the amount of money that the customers are paying the utility for the services the utility is no longer providing. I speak to you with some experience in this business, as I was not only responsible for rates and tariffs at Elizabethtown Gas, prior to coming to Enron, but I have over 15 years experience in the natural gas business designing rates and tariffs.

SENATOR LITTELL: Can I jump in for a minute?

SENATOR INVERSO: Yes, please.

SENATOR LITTELL: If you were charging \$5 a therm for gas and 13.5 percent tax under the original rate that you filed with BPU, and a competitor comes along and says, "I can supply gas to you for less," and basically what they do is back out the 13.5 percent and then add in the put-through cost, the line cost, management cost, whatever--

MR. MONTOVANO: The distribution cost?

SENATOR LITTELL: The distribution costs are -- doesn't that disappear under the proposed plan?

MR. MONTOVANO: No, because it doesn't disappear. There's nothing to adjust that distribution rate layed out in that equation.

SENATOR LITTELL: So basically what you're saying is that you can't be more competitive. You can't even be as competitive as the present utility companies, because they control the distribution cost that you would have to pay to sell that therm of gas for \$5, plus 6 percent sales tax now, instead of 13.5 percent.

MR. MONTOVANO: You're exactly right in the fact that the distribution charge is set, and it's set at different levels. And if you think about it, it should not even be equal, because we are providing services now that the utilities are no longer providing. So--

SENATOR LITTELL: Who's responsible for the product liability coverage?

MR. MONTOVANO: The product liability?

SENATOR LITTELL: Yes.

MR. MONTOVANO: The deliverability or the reliability?

SENATOR LITTELL: No. The product itself. Suppose you had a house blow up--

MR. MONTOVANO: The utility maintains the distribution system, and we will continue to pay the utility for that function. The function that we no longer feel is fair to pay the utility for is providing the natural gas -- the function of providing the natural gas to the customer. Enron is now the supplier to these customers.

SENATOR LITTELL: Can you actually buy gas at a better rate than the utilities?

MR. MONTOVANO: Well, that's what the competitive marketplace determines. If we can't, we go out of business, but we don't sell on that utility. If all things are considered equal, yes, we feel we can provide gas at a lower rate. Now, we do that from several different mechanisms of how we move gas throughout the country. But the benefit or the program isn't made or broken just on the taxes alone.

SENATOR LITTELL: Okay. But if they were only allowed to charge you the same thing they charged their own customers for distribution costs and we charged them both 6 percent, you could still compete in that market because you can buy better.

MR. MONTOVANO: If they charge our customers for the services that they are providing, then we can compete in the marketplace and pay the same tax. It will not be the same distribution charge because built into the utilities distribution charges are all the personnel and assets that go behind buying natural gas for the customers that buy gas from the utility. Right now, they're charging our customers for those people and assets. You have to peel

that out. The BPU has to be mandated to peel that out of the rates so that our customers don't pay that. And we fully support paying taxes on a level playing field with all aspects of the competitive marketplace level.

One further note, just to mention, to the extent competition fails, the whole supply-side theory behind the TEFA, that you'll have a growing economy, fails, because you'll just have monopoly services at monopoly prices.

SENATOR INVERSO: Well, let me ask this question. Obviously, you've spoken to the BPU, have you not?

MR. MONTOVANO: Yes, Senator.

SENATOR INVERSO: On this issue.

MR. MONTOVANO: Why I'm here today-- We have talked to the BPU on several occasions and negotiations with several utilities. They have recognized this problem, and they have promised us, both at meetings and in writing, that they would address the rate issues that we talk about when and if a tax change came. Why I'm here today: I'm concerned. The tax change was proposed-- First of all, the tax has been talked about for several years. The tax change was proposed in early March. We've talked to the BPU and tried to generate what we're going to do to fix this problem when the tax change comes. We have not heard back nor have meetings been scheduled. This is a task that they have to undertake immediately. Through my experience, I don't think they could get it done, if they started today, by January 1, 1998. And that's why we're asking that on the gas side, this tax change be put in place in sync with when the BPU can address the gas issue. Right now the BPU is very busy on the electric issues that are facing this State and the electric restructuring.

SENATOR INVERSO: Has the BPU indicated to you that they favor looking at peeling out the cost which should not be perfectly allocated to distribution tariffs?

MR. MONTOVANO: Yes. In a letter from the Director of the BPU, Mr. Chilton, he recognizes the need for the BPU to review and address the tariff issues, as he calls them, which I've reflected here.

SENATOR INVERSO: Right.

MR. MONTOVANO: When and if new tax implementation comes-- Again my concern is the tax issue is here, it's being discussed, and there's no avenue at the BPU for us to act today. Again, with my experience in designing these rates, it takes time. There are four gas utilities in the State that would have to be looked at, and the staff of the BPU has limited resources to do that.

SENATOR INVERSO: Okay, well, that's something that we'll have to take up with the BPU, I think. Your points are understood, and we'll have to pursue it with the BPU and see what they say.

SENATOR LITTELL: Senator, for your information, I'm having Aggie keep notes on all of these issues, and she's going to write up a single memo with everybody's requests on it.

So we will follow up on it, and I thank you very much for your coming here and testifying.

MR. MONTOVANO: I'd also like to offer my support and expertise in any other further information that you may need on this issue.

SENATOR LITTELL: Thank you.

Everybody is still left here waiting to talk: William Laing, New Jersey State, AFL-CIO; followed by Jon Spinnanger, Bell Atlantic; followed by Michael Egerton, New Jersey State Chamber of Commerce; followed by Hal Bozarth. Let's see if we can't move things along.

Not yet, Hal, you're about fourth in line here.

Okay, gentlemen.

WILLIAM L. LAING: Good afternoon or close to good evening, Senator, and I appreciate the opportunity to speak. What I'm not going to do to your, I'm sure, pleasure is read from the prepared text. I do apologize for the pen marks. My printer broke down, and not being a technician, I was unable to fix it. They're minor. The first thing I would like to try to do is refocus what we're here for.

To my left, I have a couple of constituents of mine. Dan Nickle, he's from the U-3 Council of the IBEW, representing General Public Utilities. Next to him, I have Bruce Flaemig, from Local 210 of the IBEW with Atlantic Electric.

The AFL-CIO and aggregate represents around a million people -- working people -- in New Jersey, as you well know, each one of them with a family. The reason I would like to refocus this is, my impression is this was GRFT legislation, and if we wanted to try to fix everything from rates for gas and everything else to maybe even a bond issue or two, we might be able to do that here. But I don't think everybody wants to hear all of that.

So I'd like to focus on the GRFT part of it. One of the things that's a little disturbing -- it's not in my written testimony, but I absolutely

would like it part of the record -- is Section 69.b, dealing with the personal property tax on the telephone companies.

There is no question that the municipalities are going to lose money in some respect if you drop a GRFT tax by 6 percent on certain products. But when we're dealing with the business personal property tax and telecommunications equipment and having that only apply to three companies -- the way I read this, the existing companies were Balley, Sprint, and Bell Atlantic -- and anybody else who gets involved in the local service would be exempt in the future is kind of ridiculous. That's the way I read this.

We put them at a competitive disadvantage. You keep hearing a level playing field, and I suppose depending on where you're standing on the field tells you whether it's level or not. Our view is that would put the existing companies at a competitive disadvantage as opposed to leveling the field out. So we would want to see that gone. It doesn't belong in this. Get it out. Let's deal with the GRFT tax.

Bill features: You've heard a lot of data on it, and basically we support it as written, other than that prohibition that I talked about, but I would like to talk about real quick is safety, quality, and those kinds of things. When it comes down to the existing system, distribution and everything else, generation, I don't think you have a safer, more quality-oriented group than we have with our utilities today on the generation of power.

I ask if people feel more secure, as the airlines deregulated, flying today than they did before with planes that are older than they ever were, and on and on like that. If that's where we're headed with safety in the utility industry, I say that's down the wrong road. So we have to be sure that as we

deregulate, those things stay there. Our workers are the safest in the industry. You can walk by a telephone pole today, or a utility pole as you call it, and feel fairly confident that you're not going to get hit with a jolt of electricity that is going to kill you because everything's properly bonded and things like that. So those things have to be looked at as we go forward.

Air quality in the State. Our concerns are-- We have some generating plants that are old, and we realize that. They were built for purposes. You've got people that testified they don't want to pay exit fees, they don't want to pay this fee, they don't want to pay that fee, yet the existing utilities were required, in many instances, to build plants with excess capacity, anticipated capacity, and they call them stranded costs.

Well, there's a cost of doing business no matter where you're going to be. If you're going to make an investment to build cars or whatever, I think that you have to look at it from a level-- If it's truly level, you have to have the field level for producers, users, and the municipalities.

The stranded cost is very important to us in the people sense, because that's a stranded cost that I didn't hear anybody talk about today. And those are the jobs in the generating plants that if we allow out-of-state utilities in the Midwest to generate in dirty plants, it increases the pollution that rides over New Jersey. The ancillary businesses like glass plants, etc., that use energy that's produced here, which is more expensive than the dirty energy from the Midwest-- If they're just allowed in here to sell without any modification to the GRFT tax as it is now, obviously they'll have a competitive advantage. We don't want that. We don't think it's right. To increase the air pollution here and allow the states out there to operate under less safe labor

laws, less safe laws than we have in this State-- We're proud of them. Yet to sell their energy here to us is not fair to our workers.

Somebody talked about pulling the rug out from underneath the people that made investments in plants under old rules. Well, I came out of the telephone industry. When I went for the job, I was told that, "You'll never get rich." They were right on the money about that, but I'd have a job for life being a regulated industry. Well, as you well know, that's changed. I'm sure that these gentlemen were told the same thing. People pulled the rug out from under their workers, and I'm not saying it's fair to pull it out under investors or companies, but the fact is that if the companies aren't there to make money, we don't have jobs. And what we don't want to see is all of the jobs exported to what is a little-- We don't want to turn the GRFT legislation into something which would be a mini-NAFTA, which would give a competitive advantage to the plants out in the Midwest. So we need to look at that.

If everything goes through, we'll have one last great monopoly in this State. It's probably only the Legislature, because only you guys can pass the laws. I don't think you want to allow the Midwest legislatures, Indiana and places like that, that don't want to comply or have the stringent health standards for their citizens and have the highest standard of living whether it's health, wages, or safety laws, as we have in this State--

So I would say that whatever we could do to encourage the Federal legislators-- I was very happy to hear Commissioner Tate speak about the fact that some of those things are going to be done, and I would offer our help to ensure that the lobbying is done properly to make sure that our workers absolutely, the ones that are out there in the world, are the safest in the world

and that continues to be that way. And that our residents are allowed to breathe air that's not contaminated through actions we take here to encourage the production of more pollutants by buying the dirty energy from the Midwest.

With that, before I take any questions you might have, I'd ask Dan to make a statement if he'd like. He's a lineman for General Public Utilities down in the Old Bridge area.

DAN NICKLE: Yes, thank you.

Thank you, Mr. Chairman, Senators. The comment I'd like to make is just a brief statement on an issue that Bill kind of touched, and it's the stranded cost issue. Very briefly, stranded costs, as we've discussed them today and as I'm sure you've heard in the past, is when a regulating utility was more or less forced into making investments for future considerations and increased capacity that they may not have needed at the time. In a deregulated industry, those physical facilities may no longer be a viable facility in an open market.

Under the new law, these utilities are going to be allowed to recover -- over a controlled period of time, they are going to be allowed to recover those costs, hopefully. And the one thing, like Bill said, that we didn't hear today is the people that we're going to lose -- that could potentially lose their jobs once the closing of those plants take place.

I just want to mention that I work for GPU. The system council, Youth Free, represents approximately 1600 to 1700 bargaining unit employees. I would say close to half of those employees are employed in our generating facilities. Now, in a deregulated industry, once those plants are forced to close

because GPU is looking to outside entities to purchase their power from, what we'd like to see is any legislation that's put forth concerning the deregulation of the industry contain some sort of language that concerns the recovery of stranded costs as it pertains to those employees, whether it be the retraining of those employees or some sort of job search program for the misplaced employees or, as a last resort, some sort of severance packages.

Anybody who's done their homework knows that in California, Michigan, Pennsylvania, the legislation that was drawn up had very vague language that pertained to the recovery of stranded costs as it pertains to displaced employees. It made statements like: The utilities will be allowed to discuss with their bargaining unit employees the possibility to recover stranded costs for displaced employees. We'd like to see something like that, but we'd like to see something a little more concrete. We're not looking for job protection. It would be impossible to expect everybody to say, "Okay, you guys are all going to be guaranteed your jobs at a deregulated industry." That's just an impossibility.

But what we'd like to see is that the quality, skilled labor that's been brought forth over the years in a regulated industry, that those people be shown some sort of consideration when all of a sudden, in a deregulated industry, when they're not a viable asset anymore -- say, "Well, I'm sorry, you're just out on the street." We like to see some sort of language in the legislation that does something for these people that have given the last 20, 30, 40 years to these utilities and have become skilled in a certain field, whether it be plant workers as far as maintenance guys, mechanics, or boiler workers.

These people are ratepayers. They're voters. They're taxpayers. If they lose their jobs, they're not going to be able to pay the taxes.

We talk about hopefully, in a deregulated industry, we'll be able to attract more businesses to come in. We'll be able to place those employees. That's wishful thinking, and we hope that that happens. I'm an elected official in my municipal, and I hope that that happens. But to rely completely on that is unreasonable. I just hope that the legislation, when it finally does come down, shows some consideration for those potential displaced employees.

Thank you for your time.

MR. LAING: Bruce.

BRUCE E. FLAEMIG: Yes. My name is Bruce Flaemig. I'm a Senior Communications Tech with Atlantic Electric. I'm in Local Union 210 of the IBEW. You have a copy of my testimony, so I'm not going to repeat all that, but I will say a few things. I am glad to be here. I'd like to thank you for allowing me to testify here.

As a citizen and member of Local 210, I support the Senate Bill No. 31. It will lower the New Jersey customer gross receipts and franchise tax burden by approximately 45 percent upon full implementation. This will allow for economic development and fair competition of utilities in and out of the State, while ensuring no further decline of energy tax revenues to municipalities.

Competition is good for the State and its people. As a consumer, I would like to pay a fair price for clean energy. As a taxpayer, I do not want the burden of increased taxes due to unfair competition. As a worker I want to work in a fair, competitive environment.

One thing that I would like to say, as far as stranded costs are concerned, is there has been some mention of concerns for the investor with the stranded costs. I've invested my life and my family in the State of New Jersey working for a utility. Now that job is at risk. I've worked in the utility industry and for the authorities for over 16 years in the State of New Jersey. I would really urge you to consider the workers when you do come to a decision on what you will do with this. I'd like to thank you very much for giving me the opportunity to participate in this procedure.

SENATOR LITTELL: Thank you, sir. Thanks to all three of you. We will certainly keep your comments in mind. I don't know the answer to protect all of those workers, it is very difficult. It will not happen overnight. It isn't going to be easy to control, but we will take a look at it. We certainly-- Maybe we can write some language in there directing the companies to develop a plan.

Thank you.

MR. NICKLE: Thank you.

SENATOR LITTELL: Jon Spinnanger, Bell Atlantic. A man of few words.

JON P. SPINNANGER: I will be very quick, very brief, because I know that you can all read.

Thank you very much, Mr. Chairman, and members of the Committee. I will not read my testimony in deference to the time. Let me say this to you, however.

Bell Atlantic-New Jersey is very supportive -- totally supports -- in the gross receipt and franchise tax reform initiatives. We are most anxious to

see this legislation go through the process and be signed into law. The economic development future of New Jersey hangs in the balance, and we know that there has been a tremendous amount of work done by not only the Legislature and this Committee, the Assembly, and of course, the Treasurer's office, and the BPU.

There are some concerns which we have outlined to you in both our testimony and in subsequent correspondence. We feel confident that we can address these issues subsequent to signing this piece of legislation into law. There are some important issues out there, Mr. Chairman, but they can be taken up separate, they don't have to be involved in the legislation right now.

We would ask that the bill be passed without amendment, to the extent other than technical amendments, but we certainly want no significant amendments to the sections that affect telecommunications. There are issues that should be explored by all parties, and we are willing to defer those issues until after this is signed into law.

SENATOR LITTELL: What about the one that was raised by the gentlemen just before you? He said, "Sprint United, Warwick, and Bell Atlantic are at a financial disadvantage."

MR. SPINNANGER: Yes, what he was referring to is, of course, the personal property tax which is paid directly to municipalities by local telephone companies. Now, as the local telephone exchange business becomes competitive -- which it already is and is going to become increasingly so in the coming months-- We're not talking in some very distant date, we're talking in the coming months-- We, of course, pay a personal property tax to municipalities. Those long-distance companies who are entering the local

market are not subject to that tax, and you could argue whether or not it is appropriate that they should be subject to it or not.

I'd rather give you an example that I just encountered today, I think it illustrates the point very well. It was an announcement that my employer will be shortly offering high-speed data access through a technology that we are going to be implementing. If you buy Internet access from Bell Atlantic -- high-speed data access from Bell Atlantic -- it's subject to the State sales tax. In that same article, Mr. Chairman, there was reference to a cable television provider that also offers high-speed data access at the present time -- you can actually buy it right now -- and it sells for about \$40 a month, and it is very, very fast and is very good service. That service is not subject to the State sales tax. They are identical services, but we have a disparity depending on who you buy it from. Those are the kinds of issues that we would invite your Committee and the Legislature to review, subsequent to the enactment of S-31, which, of course, we support.

We don't want to get tied up on those details. We are willing to wait until after this one goes through, and this is certainly -- as the market becomes totally competitive, it is certainly a very appropriate public policy subject for extensive dialogue and debate.

SENATOR LITTELL: Well, I'm a little surprised to hear you say that, because once you lose those customers, they are very hard to get back.

MR. SPINNANGER: Absolutely true. We are vitally concerned about that.

SENATOR LITTELL: Well, if we can fix it here, why shouldn't we fix it then?

MR. SPINNANGER: Well, we provided you with a copy of the amendment that we've asked for on Section 60. We provided that, also, to the Assembly Committee, and we would be delighted if the Committee would favorably consider the amendments which we have provided to you. We have also provided extensive technical amendments for the Committees' consideration.

SENATOR LITTELL: We'll put it down and take a look at it.

MR. SPINNANGER: Yes, sir.

SENATOR INVERSO: Jon.

MR. SPINNANGER: Yes, sir.

SENATOR INVERSO: Jon, didn't I hear you say in the beginning of your testimony that you favored the bill without amendments?

MR. SPINNANGER: What I'm saying to you, Senator, is that if our amendments-- If the telecommunications disputes are going to significantly delay the enactment of S-31, we would just as soon see the bill enacted as written and we'll take those issues up later.

We have provided, for your information and consideration, amendments that we would seek, but we can seek them in subsequent legislation. We're trying to be as flexible to the Committee and to the calendar, quite frankly.

SENATOR LITTELL: Thank you very much, Jon.

MR. SPINNANGER: Thank you very much, Mr. Chairman.

SENATOR LITTELL: We'll take a look at that.

Michael Egerton, New Jersey State Chamber of Commerce.

MICHAEL EGERTON: Thank you, Chairman. I will also be brief and refrain from reading my testimony. I guess, essentially, what the State Chamber is looking for, as an end result, from S-31 is -- I guess the bottom line is -- lower energy costs for all of our members. When I say all of our members, Chairman, I'm talking about your mom-and-pop facilities that are members of the State Chamber, as well as our large industries.

I'm sure you've heard, time and time again, that if we fail to change with the rest of the nation, businesses will view the issue of energy costs as just another reason to relocate, which will then mean that the loss in revenue will be made up by those who decide to stay here in New Jersey.

Obviously, we commend the leadership of both Senator DiFrancesco and Inverso, and the BPU President Tate, who are all involved in introducing this legislation that involved countless meetings, long hours, and hard work that, in the long run, will help bring New Jersey into the next century.

We'll continue to monitor this measure as amendments are suggested and proposed, especially if such amendments will have an impact on the overall business community.

Thank you for the opportunity to express our views, Chairman.

SENATOR LITTELL: Thank you very much. Are there any comments or questions? (negative response)

Thank you.

Hal Bozarth, Steve Gabel, Clark Hoffman, Coalition for Competitive Energy.

HAL BOZARTH: Thank you, Mr. Chairman. We appreciate the lateness of the hour, and we'll try to respond accordingly.

We're here on behalf of a fairly large group called the Coalition for Competitive Energy. It's comprised of a whole lot of people. Let me just give you four or five or six to give you an idea. The members run from American Home Products in Bristol Myers Squibb; and du Pont is with me here, to my right; General Motors, Tosco, Mobil, Monsano, Princeton University, the School Boards Association, School Business Officials, other independent institutions of higher learning, and basically the consumers of electricity in what we hope will become a competitive and a much cheaper market.

I'm going to make one major point, and then I'll ask Steve Gabel, the Coalition's expert on these issues, to elucidate on the kinds of changes that we would like to see in the bill, without which we don't think the major issue here will be reached, which is lowering the cost of electricity to the whole range of customers, all of them, including residential.

It's not necessarily the 13 percent tax which makes New Jersey have the seventh highest cost of energy in the nation, it's the cost of the energy which we must buy here in New Jersey. We're hopeful the market will open up for the simple reason that we won't continue to bleed manufacturing jobs, which can't afford to stay here, because of the high cost of the energy. While this is a tax bill -- and I understand the fundamental needs to straighten the situation before we move to a retail competition -- I would like to say to you that we shouldn't rush the judgement on this kind of thing by raising taxes on people. Our amendments seek to stop the increased taxes that the members in our Coalition will be faced with if the bill is passed in the present form.

Some people call this a move to level the playing field. I call it exactly what it is, tax and spend. For every time you heard from the folks on the other side about leveling the playing field, it was exactly that number of times when they refused to tell you that while some people don't pay the tax now, they pay something that the monopolies don't pay, and that's property tax, corporate business tax, and those are two huge numbers. To equate those two with the gross receipt taxes is quite unfair.

We would love to have a leveled playing field and we sure as heck don't have it. This bill continues to unlevel the playing field by increasing taxes on all sorts of people in the consuming end of this argument. We don't think that's what you're about, increasing taxes, and we would like to tell you the four amendments that we'll need to this bill to make sure that taxes aren't increased, and then Clark Hoffman, from du Pont, will tell you one specific example, in his plant and what happens to the competitiveness of that Salem County Plant.

Steve Gabel will briefly tell you about the amendments that we would strongly urge your consideration.

STEVEN GABEL: Thank you, Hal, and good afternoon.

I wanted to quickly outline four of the larger amendments that we've talked to some of the sponsors about, which directly go to the issue that Hal talked about in terms of economic competitiveness.

The first of those relates to the taxation of energy that's produced and used on-site. The legislation appropriately exempts that type of use from taxation but then adopts a very restrictive definition of what constitutes on-site use and requires that the energy not cross a property line or a public right-

of-way. Many of these businesses and institutions are on sites which, of course, cross property lines and cross public right-of-way. That type of provision, in the legislation, would be very restrictive and really counterproductive to the intent of the legislation, which I believe was not to tax energy that's produced and consumed by one business or one institution.

The second area, which was the subject of discussion by several other of the people testifying today, related to the taxation of natural gas, which flows into an industrial or institutional cogeneration site. The electricity that is produced from those sites is used on-site, and the area of debate is whether the gas flowing into those facilities ought to be taxed. Today, and for the last 14 years or so, that gas has not been taxed. It was a subject of legislation in the early 1980s, which exempted gas used for cogeneration purposes from taxation. That law, back then, had a sound policy base, and that is that this type of energy production, cogeneration, not only improves the economic climate in the State of New Jersey, but provides substantial environmental benefits. The nox-emissions from these facilities are a factor of 10 times to 20 times less than emissions from the average utility power plant in the region. So, when you provide this exemption, you also provide substantial environmental benefit to the State in reaching its Clean Air Act goals.

The arguments for the exemptions were strong in the '80s. They are probably even stronger in the '90s, now, with the substantial increase in pressure from the Federal government to clean up our air. So we would recommend that you not get into a debate of grandfathering natural gas use and you simply continue the exemption that currently exists in the tax code.

The other area is natural gas use for a standard process use, standard commercial or industrial use. The legislation contains what we call a poison pill. That is, if you switch your supplier at any point in time, you lose any sort of grandfathered status that you might have otherwise had. This is clearly anticompetitive and we think should be dropped from the legislation.

Finally, there was some discussion earlier about appropriate grandfather dates. In general, we recommend against retroactive grandfather dates and try to make the grandfather date effective with the date of the legislation; then, there is no uncertainty as to notice two different stakeholders in this process.

A few other areas that I wanted to touch on briefly. One relates to--

SENATOR LITTELL: Excuse me, Steve.

MR. GABEL: I'm sorry. Yes, sir.

SENATOR LITTELL: I don't mean to cut you off, but do you have these things written down so we can give them to staff, because you are rattling off a lot of issues and they can be dealt with at the staff level. It's a little hard to follow. I tried very hard.

MR. BOZARTH: We have a package ready for staff.

SENATOR LITTELL: Yes, we do have a package.

MR. GABEL: The other two issues that I wanted to touch on briefly, one relates to the comments that were made earlier by the Ratepayer Advocate relating to how to tax natural gas. I believe their comments really were evidence of a misunderstanding of not only how this legislation is supposed to work, and that is, to provide that taxation occurs at the end of the

transaction process, at the retail level, and not at the wholesale level. So there is no benefit that's being conferred on independent power producers. It's simply the logic of the tax regime that's being adopted that taxation occurs when the electricity is sold at retail and shouldn't be double taxed when the gas is consumed to produce that electricity. I think it was also based on numbers that were clearly erroneous. They relied on some documentation on stranded cost calculations that were produced by the electric utilities about a year and a half to two years ago, and those numbers themselves are utility numbers, and if you go back to the source document, the utilities themselves do not even take ownership of those numbers. So they are really putting a policy proposal here today that didn't have a base.

SENATOR INVERSO: Steve, can I object. Are you talking about the ad valorem?

MR. GABEL: No, the second piece. The conditional treatment of taxation of natural gas and their reference to IPP contracts being 33 percent to 50 percent of the State's stranded costs.

SENATOR INVERSO: Okay, because I think what they were saying was that there should be some incentive, perhaps, to have the IPP sit down with the utilities to see if they can renegotiate, lower that burden, so that by doing that they would lower the stranded cost.

MR. GABEL: Right. What I'm indicating is that the numbers they used were not only stale and inaccurate, but no one is taking ownership of those numbers, not even the people who produced them.

Finally, some earlier witnesses talked about the departing load tariff of PSE&G and decided the very clear economic impact that it had on the

Tosco Refinery and GM. There is some very clear regulatory reasons why that should be denied. It's discriminatory. It's being applied only to customers who go to inside-the-fence cogeneration and not being applied to customers who engage in energy conservation or customers who move out of the State of New Jersey or move to other service territories. So it has severe discrimination problems and I think also misapplies what the notion of stranded cost is, which is a cost that occurs when retail wheeling occurs. We have no retail access today. This is not a stranded cost which should be a subject of a special charge.

That really summarizes where we are. Senator Littell, we have provided to the sponsors, and I think to some of the staff, a much more detailed summary of what I talked about today, and I hope that will be helpful. In the case any of your staff does not have it, we'll get that to them.

SENATOR LITTELL: Thank you.

SENATOR INVERSO: Senator. That first issue of the property municipal lines, we have to address that. That, clearly, was not the intent of the language to penalize someone, such as Hoffman-LaRouche, to prohibit them from dealing within their own organization that happens to straddle two lines. That one, we need to address. The processed gas is something that requires additional debate. As far as the grandfather dates, it would make it cleaner, it seems to me, I would agree with you. I don't know what we would drop by doing that -- by moving from the March date of 1996 to something current. But that strikes me as cleaner, but we'll take a look at these again, very closely, in the Committee.

Thank you.

CLARK HOFFMAN: My name is Clark Hoffman. I represent the du Pont Company Special Chemical Business that has a major facility located in Salem County and employing, at this point in time, about 2000 people.

I was pleased to hear Senator Inverso, as we had discussions on this before, talking about addressing the property line situation, because that would put us in an in tenable position of being one of the few inside-the-fence cogeneration plants in the State that would end up paying increased taxes rather than staying down at the status quo. So I'm pleased to hear that that will be addressed.

The second point concerns, basically, what I think you need recognized is a policy change within the State -- as a matter of fact within this administration -- and that comes to the taxing, eventually -- when I say eventually, a phase-in by at least 2003 of unbundled natural gas. Commissioner Tate testified to the fact that in 1994, in order to encourage competition under this administration, major corporations were encouraged to go forward and purchase unbundled natural gas. That decision is hardly three years old. Our concern is that the bill, as written in Section 34, would phase this out by 2003 and will result in, therefore, our getting about a \$300,000 a year tax increase, depending upon how the phaseout occurs and on what our base load is.

What I'd like to point out by that is, number one, it is a policy change, number two, it will be a tax increase for us, and number three, it makes it very difficult for any corporation to make investment decisions in facilities that are energy intensive. This natural gas is used as a feed stock and goes into chemicals that feed forward into our Kaplar and our Nomex line of

products -- for those of you who heard of those brand name products. We anticipate significant growth, especially in the Kaplar line. That means, sooner or later we have got to make investment decisions on building back some of the other lines and building other plants.

When the State puts us in a situation of uncertainties-- The House can attain tax policy over a period of one administration in three years -- it causes us concern, and I think it will cause you all concern if you're figuring on maybe putting in a \$100 million or \$150 million plant that's good for 25 years or 30 years.

So I would like to offer that we think that should be amended, and we should continue to derive the benefits that were granted to the industry people who purchased natural gas starting in 1994. I'd be happy to answer any questions.

Thank you.

SENATOR LITTELL: Mr. Hoffman, do you have your statement in writing?

MR. HOFFMAN: I don't have it all, but I did submit a letter to Senator Inverso, and I'd be happy to see that you get copies of it that cover the gist of this statement.

SENATOR LITTELL: Thank you.

SENATOR EWING: Mr. Chairman.

SENATOR LITTELL: Senator Ewing.

SENATOR EWING: Senator Inverso asked me to let you know that he referred to Hoffman-LaRouche just a minute ago and he really meant du Pont.

MR. HOFFMAN: Well, Hoffman-LaRouche has a similar problem as what we do. So either reference is appropriate.

SENATOR LITTELL: Thank you, gentlemen.

Art Maurice, NJBAA. (no response)

Adam Farrah, Union County Economic Development Corporation.

A D A M F A R R A H: Thank you very much. My name is Adam Farrah. I am the Vice President of the Union County Economic Development Corporation. I appreciate this opportunity. I think I can keep this under two minutes.

The Union County Economic Development Corporation's primary mission is to focus its efforts on retaining and attracting business to Union County, New Jersey. In order to make this occur, New Jersey must furnish a business environment that is competitive with its neighboring states, as well as the rest of the country. It is especially true when you come to the subject of energy costs.

The Union County Economic Development Corporation is in support of this energy tax reform legislation. Business in the State thrives on its ability to compete with one another based on a given company's expertise in operating within a respective market cost. One factor that should not be figured into this competitive equation is the tax expense of energy.

A tax reform will hopefully level this playing field for business and allow New Jersey to remain competitive with the rest of the nation. For example, the projected deregulation to occur in the State of New York is expected to ultimately reduce a typical large business's electric bill by at least 10 percent and possibly as much as 25 percent for larger manufacturers.

Pennsylvania is looking at a 10 percent reduction in rates across the board. You can see that it's important that New Jersey business be positioned to counter this scenario; otherwise, New Jersey may experience severe setbacks in future business retention and expansion.

We've shared some of the same concerns that you heard here today from other people. There must be protection against business being forced to pay excessive exit fees to their current energy providers should they want to change vendors. There must be assurance that utilities can recover adequate stranded investment costs from the proposed Transitional Energy Facilities Assessment, and of course, municipalities have to get enough revenue to remain stable and rival current levels so as not to affect the taxpayer by shifting the tax burden in the form of increased property tax.

It appears that the nation, as a whole, is moving in the direction of deregulation. The Union County Economic Development Corporation requests that New Jersey take a proactive role on this issue by continuing to fine-tune the deregulation process so that it is of benefit to business, energy providers, and the New Jersey taxpayer.

We thank you for your time and consideration.

SENATOR LITTELL: Thank you, sir. I appreciate it.

Mark Anderson, Municipalities for a Fair Share.

MARK ANDERSON ESQ.: Good afternoon, Senator Littell, and members of the Committee. I am Mark Anderson. I represent the Township of Branchburg as township attorney, and I am also President of Municipalities for a Fair Share, which is an organization that, for the last two decades or so, has been concerned about the revenues which currently flow to municipalities

for the gross receipts and franchise taxes. I appreciate that my patience has been rewarded this afternoon by your attention. I hope that I will reward you by being very brief.

I bring to you what I think is a simple message, and one which may get overlooked in detail that so many people are rightfully bringing to this Committee. The message is on behalf of municipalities. Please do not increase the dependence of municipalities on local property taxes. There is a connection here -- I'm not lost, I'm not before the wrong Committee -- to the extent that the tax revenues which municipalities have received from gross receipts and franchise taxes are reduced. Municipalities have only one other source from which they can regain the revenue, and that is, of course, local property taxes.

Gross receipts and franchise taxes are not an insignificant form of municipal revenue; they are, as I'm sure that members of the Committee are aware, the second largest source of municipal revenue in the State of New Jersey. The local property tax is, of course, the first.

I would appreciate the Committee considering my remarks in light of what the League of Municipalities has testified before this Committee earlier today. The League, of course, represents all of municipalities. It supports these bills, S-30 and S-31. In general, the Municipalities for a Fair Share does likewise, but we would like to highlight the twin problems that causes the bill, as it is currently written, to increase dependence on local property taxes.

The first of these has really been addressed by the League in its comments, and that is, the starting point at which revenue is set for distribution. The League has made a recommendation that the starting point

be increased from what is now proposed to the 1995 revenue -- of course that was the high watermark of distribution to municipalities. I will not belabor that point because I think the League has adequately addressed it.

The other point which I am concerned is being lost in the detail is the question of inflation. As inflation goes on -- and it will, at least to some extent -- it will decrease the value of the revenues which are proposed to be distributed to municipalities. If we take a -- what I consider -- a fairly conservative inflation rate of 3 percent a year over 10 years, it would reduce the amount of distribution now proposed at \$730 million to the equivalent buying power of \$538 million, which is, in buying power, a reduction of \$200 million. That's a lot of reduction and 10 years is not all that long a period of time. The difference -- that reduction in buying power -- will be made up by municipalities under the current circumstances by local property taxes. They have no alternative. So, in 10 years, the local property taxes will have to go up to the equivalent buying power of \$200 million, and there is no way around it.

There is a resolution, however, to this. The resolution is to provide some form of indexing or compensation for inflation for the revenues that are to be distributed to municipalities, and in particular, it would be the suggestion of Municipalities for a Fair Share that that indexing should be tied to the index rate for the local municipal property tax cap. The State, of course, mandates a limitation on increases in local property taxes based on what the State calculates to be the inflation rate. It seems to me entirely appropriate that if the State is going to limit on one hand, based on inflation, that they give back with the other hand.

So the specific suggestion I bring to you is that the revenue distribution in this replacement be increased for inflation by the same rate as the cap rate index is established each year in the State of New Jersey.

That's all I have and I thank you.

SENATOR LITTELL: Thank you, Mr. Anderson.

I understand that cost of living increases, but those are the kinds of things that get us in trouble someplace down the road if we don't have the money. I will tell you for one-- Although it is fair to do what you suggest, I'm not sure that the growth will exist to pay that bill. I would be very concerned about doing that right up front.

MR. HOFFMAN: I appreciate your concern, Senator. The result, though, of ignoring that is, as I say, an increasing dependence on local property taxes. It is inevitable. I would also point out that municipalities have always enjoyed a system, a mechanism under the taxes which provides growth, not necessarily and it never has been tied directly to inflation, but in the old days -- and I'm old enough to remember them -- when this was-- In fact, the energy taxes were gross receipt taxes before the unit tax was brought in. Of course, it was tied directly to the amount of revenue that the utilities took in. One always expected that the long term would bring growth in that. When the unit tax was brought in, in the '80s -- for reasons which I don't think we need to hash over now -- again, while it was tied to the sale of units of energy, there was still an expectation that the State grew, the revenue base would grow, and distributions to municipalities would grow. Indeed that has been true. That has been interrupted only by, of course, energy competition.

SENATOR LITTELL: I'm not sure that is true in this case because you're talking about a much more competitive marketplace and the marketplace would be driven by cost, and if competition creates a lower retail sales price and the tax is less, then it's not going to have the kind of growth that it's had in the past.

MR. ANDERSON: I understand that. My point is that in the many, many decades that these taxes have existed, this will be the first time in which municipalities will not be promised some degree of offset by some kind of mechanism for the expectation that dollars will be worth less over the period of time. It was before there had been a mechanism and it seems to me appropriate that there continue to be some mechanism.

SENATOR LITTELL: Thank you very much, sir. Are there any comments or questions? (negative response)

Now we have Barbara Thurgarland, Steve Scalera, James Kenny, and Cary Hinton.

Do we have everybody on your list?

BARBARA THURGARLAND: Yes.

Good afternoon, Mr. Chairman, and other members of the Committee. I would like to thank you for the opportunity to testify on S-31 this afternoon.

I'm Barbara Thurgarland and I do the legislative affairs for AT&T. Here on the panel with me, this afternoon, is Steve Scalera, who is from our Tax Department, who will discuss some tax issues; Jim Kenny, who is from the Tax Department for MCI; and also Cary Hinton, who is from Government Affairs from Sprint.

I just wanted to say that we're here to present a unified position on three issues -- actually two issues -- in the bill and one other issue. I'll discuss the right-of-way issue, which is Section 69 of the bill. We also have some concerns on the personal property tax issue, which is Section 60; however, what Bell Atlantic is proposing, and there are no amendments to Section 60 to personal property tax, we will support that section.

The third piece that I want to discuss, very briefly, is the competition in the local exchange marketplace. In deference to the time I did pass out a package. I don't have prepared written testimony, but I do have a package of information, and what I would like to refer you to is the first two pages of the package, which talks about the right-of-way issue.

The issue really is that some local municipalities are attempting to impose gross receipt-like taxes on carriers requesting access to public right-of-ways, and we did hear what the League of Municipalities had to say here today. Not only do they want to retain that right, they also want community benefit rights and the right to impose personal property taxes on new entrance into the local exchange marketplace. The only thing that is going to succeed in doing is driving businesses right out of the State.

Our concern on Section 69, in both bills, the Senate bill and the Assembly companion bill, is the wording that would encourage these and other municipalities to pursue such taxing policies, which we believe are in violation of the Federal law, State law, and the sound economic policy for the State of New Jersey.

What we are requesting, as you will see in the second section, the proposed change, is to have a few words amended from the language which

will, in effect, protect all energy and telecommunications companies and not allow the municipalities to levy any fees, assessments, or taxes for use of any of their right-of-ways. The rationale for this is that-- The way the wording is today, we believe, is in violation of the Federal Telecommunications Act, which states on the second page that "all access to public right-of-ways require fair and reasonable compensation for telecommunications provided, but it must be on a competitively neutral and nondiscriminatory basis." The way the wording is right now it says, Clearly discriminate against new entrance into the local exchange marketplace.

We also want to ensure consistency with existing New Jersey law that does not allow such municipal taxes. I am, of course, supporting the Governor's Economic Management Plan, which is not to create any new taxes that discourage investment from New Jersey.

The forth reason is that in order to keep New Jersey competitive with other states, like Pennsylvania, that do not already allow such right-of-way taxes. So, again, we are requesting that that language in Section 69.a be modified.

Now, I would like to turn it over to Steve Scalera, who will talk about some of the background on the personal property tax issue.

STEVE SCALERA: Mr. Chairman, other members of the Committee, I am here today to speak to, specifically, Section 60 of S-31 which deals with personal property tax.

You have copies of my written testimony, and attached to that I have included some charts and graphs and historical summary of the property tax, as it relates to telecommunication companies, in addition to the historical

summary of telecommunications taxation, in general. I think that is important because, when you talk about personal property tax on telecommunication companies, you can't look at it in a vacuum because there are reasons why local service providers are taxed the way they are and the way long-distance service providers are taxed the way they are.

In the interest of time, I will go through and try to paraphrase my testimony, just to hit the high points and hopefully get across some important points that I think are worth noting.

As Mr. Spinnanger pointed out, currently, local service providers are subject to the local personal property tax in addition to other public utility taxes. Currently, long-distance providers are not subject to the local tax, but they are subject to a series of other general, nonutility business taxes in the State. It is critical to understand that there has always been, and there currently still is, a reason why that disparity exists. That reason is competition.

Long-distance providers operate in a totally competitive marketplace and are taxed, essentially, as any other general nonutility business. Local service providers continue to operate essentially in a monopoly environment and are taxed as utilities.

The amendments proposed by Section 60 of this bill, in essence, would ensure continued application of all of the personal property tax to incumbent local service providers until their share of the marketplace drops below 51 percent. We support that amendment for the following reasons:

First, it maintains a monopoly tax on the monopoly provider. The divestiture of AT&T in 1984 did not automatically create competition, but rather facilitated an environment in which competition could be created. In

fact, AT&T remains subject to various forms of utility taxation up until 1990 when it was finally taxed as any other competitive nonutility business in the State.

Second, we believe that it provides a stronger incentive for incumbent local service providers to open up their markets to competition. By eliminating monopoly tax without first eliminating benefits of monopoly status, you also eliminate all incentive to promote competition in the local service market. Requiring incumbent local service providers to pay this tax until true competition exists in the local service market represents a fair tax policy and will serve as a financial catalyst to stimulate competition.

The balance of my written testimony addresses efforts and, also I believe, pending legislation in the Assembly to extend this local personal monopoly property tax to all providers of telecommunication services. Without getting into too much of the detail behind the bullet points here, I think I have provided adequate support for what our positions are on that. I will just go over and highlight major points of why we don't agree with that proposal -- why we think it's wrong -- and I'll be happy to answer any further questions or provide you with any degree of detail that you may want on that issue.

First of all, no other competitive nonutility business in New Jersey is subject to a personal property tax at the State or local level.

Secondly, extending application of this tax to competitive telecommunication providers would discourage investment and hinder competition.

Third, it would mitigate the benefits of recent changes to the corporation business tax. I am referring to Assembly Bill No. 89, which recently made substantial changes to the way in which the income of a multistate business is allocated in apportion to New Jersey for income tax purposes. It does not make sense to offset the incentive created by the changes to the Corporation Business Tax Act by now imposing a tax on your investment in the form of a property tax.

Fourth, it would be contrary to the State's historical treatment of competitive nonutility companies. What I am referring to here is the divestiture of AT&T in 1984. The Legislature, at that time, did not respond to that diverging competition by treating new entrance as utilities. They responded by an act in tax legislation that treated them as the competitive businesses that they were.

Finally, we have heard a lot about the proverbial level playing field, and it is our position that creating that level playing field does not mean subjecting competitive businesses to a monopoly tax. The intent of the Telecommunications Act of 1996 was to create competition, in all markets, so that consumers will benefit for more advanced, affordable, and accessible telecommunications services. Accordingly, we believe, tax policy should recognize and support the migration from a monopoly environment to a competitive environment and not the other way around.

In closing, I would just like to note that AT&T wholeheartedly supports open and true competition in all telecommunications markets, and we advocate equal taxation of all the companies providing services in those

markets. However, until open and true competition exists, AT&T strongly believes that monopoly providers remain subject to monopoly taxation.

On behalf of AT&T and, more importantly, all consumers of telecommunication services in the State of New Jersey, I urge you to support the provisions of Section 60 of Senate Bill No. 31.

Thank you.

JAMES N. KENNY: Mr. Chairman, my name is Jim Kenny. I am Senior Management of Tax Legislative Affairs for MCI. I will be very brief in my discussion points on Section 69 and the personal property tax. You have my written testimony. Section 69 protects only local exchange companies -- the monopoly local exchange company -- in the State of New Jersey, currently. It does not protect MCI, Sprint, or AT&T from a municipality tax, only the monopoly Bell Atlantic or United up north. This violates the Constitution, and it violates the spirit of the Telecommunications Act of 1996.

With regard to that, what we would like is -- you have the amendment in front of you as to what we think the amendment should be -- to put a period at the end of telecommunications companies. With regard to the personal property tax, I agree, pretty much, with everything that Steve said regarding the local personal property tax that the monopoly local exchange companies are subject to.

I don't think the answer to the question is to impose a monopoly tax on new entrance, it's to solve the problem. When competition exists -- and it doesn't exist today in the State of New Jersey in the local exchange industry -- when it exists, I think we should look to getting rid of a monopoly tax in

finding a different revenue source, if need be, for the municipalities to continue with.

Thank you.

SENATOR LITTELL: How about we just figure out how much we need and we'll send you a bill and you collect it any way you can. (laughter)

CARY HINTON: Thank you, my name is Cary Hinton. By way of introduction, I am Staff Director for Sprint Communications Company. I represent Sprint in the 14 states that comprise of Bell Atlantic and the NYNEX service areas.

Initially, let me state that we concur with the comments that have been offered by my compatriots from AT&T and MCI, and in the interest of brevity, I would only like to highlight two or three points.

First is, I would like to draw your attention to -- actually one of the items that's been provided to you by AT&T -- it's a study that was jointly funded by AT&T, MCI, Sprint, as well as several other companies, and it was the first study that has ever been done by a third-party objective source of the status of local competition in the State of New Jersey. That is entitled, for your edification, *An analysis of Local Switched Services Market Share in the Bell Atlantic-New Jersey Region* and was prepared by a company known as Atlantic-ACM. It was based on a survey not only of competitive local exchange carriers that are providing or have petitioned the Board of Public Utilities to provide service in the State of New Jersey, but also based on public information that Bell Atlantic has provided to the Board. All of that data is current as of the end of March.

There are three important findings that came from that study that you should understand, particularly when you reflect upon the comments and the written testimony that had been provided to you by Mr. Spinnanger from Bell Atlantic, relative to their conclusion that there is active competition in the State of New Jersey, therefore, justifying their particular tax policy proposals.

The first conclusion from that report -- not surprisingly, hopefully -- is that 99.9 percent of all business and residential lines in the Bell Atlantic-New Jersey territory are Bell Atlantic customers. The penetration by the competitive local exchange carriers has been limited to less than 30 business customers in the State of New Jersey that comprise a total of only 685 business lines.

When you look at the respective networks -- the physical facilities -- that have been constructed in the State of New Jersey by Bell Atlantic in comparison to the competitors, you will find that 98.7 percent of the operational switches in those networks -- and that is really the brains that make any telecommunications network work -- that 98.7 percent of those switches are owned by Bell Atlantic. Clearly, local competition has yet to arrive. I might also point out that even for long-distance services, as Mr. Spinnanger indicated, that we have only had barely two weeks -- from May 5 -- in which customers have had the opportunities to select their provider of what is known as Intra Lateral Long-Distance Service, sometimes referred to as local toll service. They have had an opportunity to select their carrier of choice. Even for that type of long-distance service, New Jersey has relatively little competition at this point in time.

I think one of the important points to recognize is that tax policy should really be parallel to regulatory policy. The two of them need to go hand in hand. I think, as outlined for you by President Tate from the Board of Public Utilities, that's their policy position, particularly relative to the electrical and the natural gas companies. Although he really didn't have the opportunity to go into much detail regarding telecommunication companies, there currently is a dual approach to the regulation of telecommunications companies in New Jersey, as well as at the Federal level by the Federal Communications Commission -- generally referred to as a dominate and nondominate form of regulation -- whereby the monopoly company, for example Bell Atlantic, is subject to much greater scrutiny through the regulatory process than the new entrance that proposed to provide competitive local exchange service, or even by the long-distance companies.

Unfortunately, the proposals that have been made by Bell Atlantic are being advocated on the basis that there is complete and equal competition, therefore, there is a demand for immediate tax parity, as they have characterized it. As my compatriots have indicated, for a number of reasons, tax parity is inappropriate at this time because of the monopoly status of Bell Atlantic. Specifically, I would like to address the two relevant sections, Sections 60 and 69, and I'll try to be brief about that.

First off, Section 60, as has been outlined very succinctly with regard to personal property tax. From Sprint's perspective, the proposed Bell Atlantic amendment that is contained in their written testimony would discourage investment by companies, such as Sprint, that are primarily located outside of the State of New Jersey from investing in the State. What you may

not recognize is that as companies such as Sprint and others construct facilities to be able to provide local telephone service in competition -- direct competition -- with Bell Atlantic, we have a choice of whether to locate the switching equipment -- that being the major investment for that network. An individual switch for our company will cost anywhere for half a million to \$2 million. We can locate that switch in New Jersey, or we can locate that switch in Pennsylvania or in New York and interconnect it with the physical lines and be able to provide the same local service in New Jersey. If we locate it in New York or we locate it in Pennsylvania, it is not going to be subject to a local personal property tax, but if the Bell Atlantic Amendment is adopted, I assure you that provides a strong economic incentive for us not to locate those facilities in the State. Parenthetically, there is other economic ramifications if we don't locate those facilities here and economic benefits that, therefore, would accrue to those other states.

Regarding Section 69, I agree wholeheartedly with the comments of my compatriots, that as currently drafted, by exempting Bell Atlantic from any right-of-way taxes and subjecting new entrance in long-distance companies to right-of-way taxes threatens the integrity and the viability of the provisions under the Federal Telecommunications Act and frankly invites litigation -- potential preemption -- by the Federal Communication Commission. It is blatantly unfair and discriminatory to exempt Bell Atlantic from that type of right-of-way fee and to subject us to that. Now the answer is not to subject Bell Atlantic to the fee, as well as us. The answer is to exempt both of us from that fee.

Bell Atlantic advocates that local governments -- and this is in their written testimony -- Bell Atlantic advocates that local governments need to impose right-of-way taxes on other telecommunications companies because the corporate business taxes paid by these companies, such as ours, do not get distributed to the municipalities and will not fund the energy tax receipts property tax relief fund. We don't think that the answer to that problem is to subject us all then to the right-of-way tax -- potentially from the local governments. If, in fact, there is a problem from the municipalities' perspective -- and that the Legislature concurs that there is a problem -- we would suggest the way to address it is to amend Senate Bill No. 30 to allocate a portion of the corporate income taxes that we pay to the State to have that included in the fund and therefore flowed back to the municipalities. The answer is not for us to continue to pay the corporate income tax and then add on top of that additional municipality taxes to cover presumed right-of-way usage.

At this point, I conclude my testimony, and I would be happy to answer any questions, as I'm sure my compatriots would.

SENATOR LITTELL: Thank you, Cary. Thank you to all of you, Jim, Steve, and Barbara.

We have your comments here. They are going to be considered as part of an overall review of the testimony today, and we'll let you know how it comes out.

Peter.

SENATOR INVERSO: If we didn't have 60 or 69, then you guys would be thrilled?

MR. HINTON: I'm sorry?

SENATOR INVERSO: If we didn't have Section 60 or 69, you would be very supportive of this?

MR. HINTON: Section 60 as it is drafted, 69 with an amendment.

SENATOR INVERSO: But if we had neither--

MR. KENNY: If both were deleted completely we would be fine. We would be happy.

SENATOR INVERSO: You would be extremely happy and we would have a problem. I've got \$2.9 million in my District from the right-of way under the personal property tax. That is an issue that we discussed earlier. It's a real issue that we need to -- so we can't eliminate.

Trying to bring fairness and to be competitive-- We had this discussion. Conceptionally, our fiscal policy ought to be one that is neutral with regard to favoring or disfavoring a party in a competitive free market situation. That is what we need to address here, whether indeed we are achieving that by this or whether we are not achieving that.

MR. KENNY: Senator, I don't think none of us are advocating today to eliminate first the local property tax at all. For the simple reason that the local person or property tax is a monopoly tax and a monopoly does exist and should still pay that tax.

SENATOR INVERSO: Yes, we had this discussion. Definitionally, if it is a monopoly tax, it should be imposed on those who have a monopoly, and the question is who has the monopoly, and you're saying

there is only one party that has monopoly. There is no competition, therefore, we still have a monopoly situation. I hear what you're saying.

MR. KENNY: I'll give you the example that I gave you before, out loud. The day that you can go home and decide that you do not want your local exchange company, Bell Atlantic, to be your local exchange company, if you want to switch to AT&T, MCI, or Sprint is the day that you have full -- as used in the testimony, I think Bell Atlantic -- full-blown competition.

MR. HINTON: If I might add one other, perhaps, perspective to this issue is that by extending the personal property tax to our companies, as well as to other companies that aren't represented here, you frankly are going to make it much more difficult to ever eliminate that tax. You're going to end up increasing the revenues that are going to go to the municipalities, and they will now be able to collect from us, as well as what they currently collect from Bell Atlantic. That is really the wrong direction you need to go. What's in the bill now is, at least based on the presumption that in some point in time Bell Atlantic may not have a monopoly, that there will be numerous providers of service out there, and frankly, as competition grows -- and we have seen this clearly on the interstate basis -- in effect the pie of revenues grows, too.

AT&T, when they initially opposed competition, argued that they were going to lose revenues from long-distance service. That has not been demonstrated over the last 10 or 13 years of long-distance competition. We don't believe that is going to occur at the local level. As a result of that local market growing, there are going to be revenues that will flow back to the local jurisdictions that will compensate for the loss of that personal property tax revenue.

SENATOR INVERSO: Municipalities also unhost community benefit prerogatives, which is another dimension which is not contemplated in 60 or 69. So that is another issue, and you're right, once we start providing that tax flow we're are never going to be able to alter the course. On the other hand, clearly we are looking to maintain a level of around \$1.1 billion dollars in this brand of design here. And how all of these fit together and still try to achieve some fairness in the competitive process that you are confronting is a difficult chore. But, if you have some other suggestions that can help us accommodate what we are dealing with-- Like I said, in my District alone it is almost \$3 million. If there is another way to provide for that \$3 million and, yet, from a Solomon perspective, the neutral, from a fiscal standpoint, as it relates to the competitiveness, that has to evolve.

MR. HINTON: I understand your dilemma, but I think what you have to remember, at least, the way Section 60 is currently drafted it uses a 51 percent threshold and it's going to be several years away. Bell Atlantic is going to continue with tooth and with nail to prevent a loss of 49 percent of their market share. That, frankly, hasn't happened for AT&T out in the long-distance market as much as the two of us would like that to happen and, as much as we try to advertise and market our services, it hasn't happened. We're probably talking at least the same amount of time if not longer for that to happen in the local market.

MR. KENNY: If our marketing people saw us sitting here together, unified, they would probably have cardiac arrest.

SENATOR INVERSO: Well, that's what market people should do, anyway. We're the guys that crank it out.

Well, okay, we know the issue. We'll have to put our heads together and see how best to accommodate it, and we have to have both parties sit down and revisit this. We'll follow up on it.

SENATOR INVERSO: Thank you.

(HEARING CONCLUDED)