GENERAL ASSEMBLY OF NORTH CAROLINA

Session 2009

Legislative Fiscal Note

BILL NUMBER: House Bill 1099 (Fifth Edition)

SHORT TITLE: Amend Environmental Laws 2009.

SPONSOR(S):

FISCAL IMPACT

Yes (x) **No ( )** **No Estimate Available ( )**

	FY 2009-10	FY 2010-11	FY 2011-12	FY 2012-13	FY 2013-14
REVENUES	****See Assumptions and Methodology****				
EXPENDITURES	****See Assumptions and Methodology****				

POSITIONS (cumulative):

PRINCIPAL DEPARTMENT(S) & PROGRAM(S) AFFECTED: Department of Environment and Natural Resources; Department of Transportation; Environmental Management Commission

EFFECTIVE DATE: Section 2 effective October 1, 2009. Section 4 effective retroactively to April 1, 2009. Section 3(h) effective January 1, 2010. All other sections effective when the bill becomes law.

BILL SUMMARY:
H.B. 1099 makes a number of changes to existing environmental laws across a range of areas.

Section 1 would extend the date by one year to July 1, 2010 for the implementation of water system efficiency programs by local government water systems and large community water systems in order to be eligible for State water infrastructure funds.

Section 2 would add a new section to Chapter 136 of the General Statutes (Roads and Highways) to prohibit the use of high content arsenic glass beads in paint that is used for pavement marking. This Section would become effective October 1, 2009 and apply to any contracts for road projects entered into, or any pavement re-marking that takes place, on or after that date.

Section 3 would amend the Bernard Allen Emergency Drinking Water Fund to provide that up to 50% of the funds available each year be allocated to the development of groundwater quality assessments and groundwater quality plans by the Department of Environment and Natural Resources (DENR). This section would also provide that no more than one-third of the total cost of the project may be paid from the Fund for any project totaling more than $50,000.

Section 4 would provide that city and county building inspectors may rely upon a third-party certification, provided by an applicant, that a parking lot and any bioretention area are properly designed and constructed to both comply with GS 113A-71 (Vehicular Surface Areas) and in accordance with guidelines developed by DENR. The certification must be provided under seal by a licensed professional engineer or other licensed professional that is recognized as having expertise in the design and construction of pervious parking areas or stormwater bioretention areas, as appropriate. This section is effective retroactively to April 1, 2009.

Sections 5 and 6 would do the following:
Extend the deadline for the Environmental Management Commission (EMC) to develop and implement a nutrient management strategy for certain drinking water supply reservoirs from July 1, 2009 to January 15, 2011. This section would also direct EMC to adopt temporary rules concurrent with permanent rules by January 15, 2011.

- Clarify that the rules adopted pursuant to the nutrient management strategy to reduce nutrient loading from new development be implemented no more than 30 months after the rules become effective.
- Authorize compensatory mitigation for riparian buffer loss and nutrient offset purchases in a watershed of a drinking water supply provided the mitigation or offset is performed or purchased within that watershed.
- Implement additional sedimentation and erosion control standards for land-disturbing activities in the water supply watershed effective January 1, 2010.
- Require DENR, in consultation with EMC, to identify improvements needed in the design, operation, and siting of septic tank systems in order to reduce nutrient loading from those systems to the water supply watershed. DENR must report its findings and recommendations to the Commission for Public Health and the Environmental Review Commission (ERC) by March 1, 2010.
- Require the Sedimentation Control Commission to adopt rules of statewide applicability for the control of erosion and sedimentation resulting from land-disturbing activities in watersheds of water supply reservoirs no later than December 31, 2011.

Section 7 would direct EMC to encourage local governments, landowners, and others to develop, adopt, and implement policies and practices to reduce the runoff and discharge of nitrogen, phosphorus, and sediment into the surface waters and drinking water supply reservoirs of the Upper Neuse River Basin before it adopts permanent rules to implement the nutrient management strategy for Falls Lake. The bill requires EMC, in its permanent rules, to provide credit to local governments, landowners, and others who implement policies and practices after January 1, 2007 to reduce runoff and discharge of nutrients and sediment in the Basin. This section would also direct EMC to report its progress in implementing the credit for early adoption to ERC as part of its quarterly reporting as required by statute.

Section 8 would direct the Revenue Laws Study Committee and ERC to jointly study revenue generating opportunities associated with entities of the State that are large-scale users of certain natural resources of the State. The Committee and ERC would be required to jointly submit a report to the 2009 General Assembly no later than April 1, 2010. The report must include findings and recommendations, including a proposal to generate revenue as identified by the study.

Section 9 prohibits Concord and Kannapolis from transferring water from the Catawba River Basin pursuant to the certificate approved by EMC on January 10, 2007, and signed into effect on January 25, 2007, unless DENR determines that certain conditions are met.

Finally**, Section 10** adds new Article 9, Yadkin River Trust, to G.S. 77. This Article establishes the Yadkin River Trust (Trust) as a public agency, creating the Trust's board of directors and its duties and operating procedures. It authorizes the Trust to acquire the federal license for the Yadkin River Dam and, if so acquired, to seek permission from the General Assembly to issue revenue bonds or other financing to enable acquisition and operation of the Yadkin Project. H.B. 1099 directs the Trust, if it acquires the Yadkin Project, to:

- Comply with the terms of the Relicensing Settlement Agreement with the Federal Energy Regulatory Commission (FERC) dated May 7, 2007,
- Evaluate the environmental risks posed by certain properties in the Yadkin River Valley,
- Apportion up to 25% of the proceeds from the Yadkin Project's electrical output for a regional "Power for Jobs" fund administered by the Department of Commerce,
- Make changes to retain water for certain local lakes and to provide consistent water flow,
- Utilize up to 25% of the remaining net revenue to make grants to the Community College System Office, and
- Use any remaining net revenues to fund projects to protect the Yadkin River.

In addition, the bill creates reporting procedures and conflict of interest provisions for the Trust and its officers, directors, and employees. Section 10(f) requires the Department of Justice to report by July 1, 2010, on discussions between the State and Alcoa, Inc., and other parties concerning the Yadkin Project. Section 10(g) requires the Secretary of Commerce to present a detailed business plan for the operation of the Trust on or before March 1, 2010.

ASSUMPTIONS AND METHODOLOGY:

<u>Section 1: Water Shortage Response Plans</u>

Section 1 provides for a one-year extension for local governments to implement water system efficiency programs to be eligible for State water infrastructure funds. There should be no costs associated with this section.

<u>Section 2: High Content Arsenic Glass Beads</u>

Section 2 of H.B. 1099 could impact the Department of Transportation (DOT) - State Highway System as well as municipal street systems and public vehicular areas. DOT does not currently use high content arsenic glass beads in paint used for pavement markings. However, DOT does suggest the possibility that forbidding this product could reduce the number of bids that DOT receives and possibly lead to higher costs.

No information is available on the extent to which high content arsenic glass beads are used for municipal street systems or by governmental units for public vehicular areas; therefore, the Fiscal Research Division cannot determine the fiscal impact of this change on these entities.

Section 3: Bernard Allen Memorial Emergency Drinking Water Fund

Section 3 changes the allocation and uses of funds from the Bernard Allen Memorial Emergency Drinking Water Fund. This section adds language to GS 87-98, allowing up to 50% of the funds available each year to be used to develop groundwater quality assessments. Allowing this new use of funds will result in less money being available to fund alternative drinking water supplies. Additionally, this section would provide that no more than one-third of the total cost of the project may be paid from the Fund for any project totaling more than $50,000. Under current law, the Fund may not pay for more than one-third of any project. With this change, the Fund may pay the full costs of any project up to $49,999.

Section 3 should not incur any nest costs to the State.

Section 4: Third-party Certification

Section 4 allows city and county building inspectors to rely upon a third-party certification that a parking lot and any bioretention area are properly designed and constructed to both comply with GS 113A-71 (Vehicular Surface Areas) and in accordance with guidelines developed by DENR. There should be no cost to the State for this section.

Sections 5 & 6: Nutrient Management Strategies

Section 5(a) extends the deadline for the Environmental Management Commission (EMC) to develop and implement a nutrient management strategy for certain drinking water supply reservoirs from July 1, 2009 to January 15, 2011. Section 6(a) would also direct EMC to adopt temporary rules concurrent with permanent rules by January 15, 2011. There should be no new costs related to these sections.

Section 5(b) amends Section 3 of S.L. 2005-190, as amended by S.L. 2006-259 by adding three new subsections relevant to activities in watersheds of a drinking water supply. The first new section (Section 3.(g)) creates requirements regarding compensatory mitigation for riparian buffer loss; the second subsection (Section 3.(h)) creates additional standards for land-disturbing activities in water supply watersheds; and the third subsection (Section 3.(i)) directs DENR, in consultation with the EMC, to identify improvements needed in the design, operations, and siting of septic tank systems to reduce nutrient loading. The fiscal impact of the new subsections cannot be accurately determined. There should be no increase in expenses to DENR. However, expected revenues to the Ecosystem Enhancement Program could be affected by the changes in compensatory mitigation requirements.

Section 6(b) directs the Sedimentation Control Commission to adopt rules regarding land-disturbing activities in the watersheds of water supply reservoirs. The Department does not anticipate any new costs from this section.

Section 7: Upper Neuse River Basin Pollution

Section 7 directs EMC to encourage affected parties in the Upper Neuse River Basin to adopt runoff and sediment practices in advance of permanent rules. EMC is directed to give credit for these early adoption practices in its permanent rules and to report to the Environmental Review Commission on the progress of the early adoption credit program. There should be no new costs for section 7.

Section 8: Study Revenue Generating Opportunities
Section 8 directs the Revenue Laws Study Committee and ERC to jointly study revenue generating opportunities associated with entities of the State that are large-scale users of certain natural resources of the State and report the results by April 1, 2010. The section should not have a fiscal impact for the State.

Section 9: Limit Water Transfers
Section 9 prohibits Concord and Kannapolis from transferring water from the Catawba River Basin pursuant to the certificate approved by EMC on January 10, 2007, and signed into effect on January 25, 2007, unless DENR determines that certain conditions are met. This section should not have a fiscal impact for the State.

Section 10: Yadkin River Trust

New GS 77-150 creates the Yadkin River Trust as a public agency and instrumentality of the State. The bill is permissive as to the Yadkin Trust acquiring the Yadkin Project; new GS 77-153 states that "The Yadkin River Trust *may acquire* the Yadkin Project." Any future revenues are directed to the following: environmental site assessments and remediation of properties currently or formerly owned by Alcoa in the Yadkin River Basin and other sites at the Badin Work site; a new "Power for Jobs" fund within the Department of Commerce; the Community College System Office for equipment; and to fund projects to protect and improve the health of the Rive and water quality in the Yadkin River Basin.

If the Trust acquires the license, then they must receive permission from the General Assembly to pursue revenue bonds to fund the acquisition of the Project. As the bill is written, the State would not incur acquisition costs until after such permission has been granted. However, in recognition of the potential for the Trust to acquire the Project and seek such permission, Fiscal Research offers the following estimates. **It should be noted that these estimates are provided with the qualification that Fiscal Research does not have the staff resources to conduct a thorough, independent analysis of the costs at this time. Thus, Fiscal Research has relied on data from the various parties involved in these proceedings (mainly Alcoa/APGI and Stanly County) to form a range of estimates.**

Cost of Acquiring the Yadkin Project
There is some dispute as to what basis should be used to determine the value of the Yadkin Project were the Yadkin Trust to attempt to acquire it. The FERC relicensing guidelines allow for federal takeover of a project and stipulate that the value of such a takeover would be determined as "net investment...not to exceed the fair value of the property taken, plus such reasonable damages, if any."[1] Fiscal Research notes that this section also states that FERC would ultimately determine this value. Per Alcoa's 2006 License Application, the "net investment" amount is $24,158,903

[1] Federal Power Act, 16 U.S.C § 807(a)

(2005 dollars).[2] Lobbyists for Stanly County contend that $24.2 million is thus the fair value and further contend that reasonable severance damages would be minimal, if any.

Lobbyists for Alcoa contend that severance damages would be "hundreds of millions of dollars" including the costs of replacing the assets in Alcoa's energy portfolio as well as compensation to shareholders for loss of assets and associated revenue stream. However, Stanly County contends that future potential revenues beyond the original 1958 license term should not be included in the calculation of severance damages.

Additionally, Alcoa states that it has invested approximately $67 million in the Yadkin Project since the license application was submitted in 2006. $25 million was spent on relicensing and $42 million was spent modernizing facilities including the Narrows Powerhouse, the High Rock Powerhouse, and circuit breakers and other equipment at the Falls and Narrows powerhouses. Alcoa contends that its "net investment" is now closer to $91.2 million.

Setting aside the issue of "net investment," Alcoa contends that Federal recapture of the license is no longer possible, and thus the only way for the Yadkin Trust to acquire the project would be through direct purchase from Alcoa or condemnation. Under either of these scenarios (although it should be noted that Alcoa has stated that it does not wish to sell the Yadkin Project), "fair market value" could be used to determine the purchase price. Alcoa acknowledges that it has not had an independent appraisal conducted, but it estimates the fair market value to be in excess of $500 million. Proponents of the Yadkin River Trust refute the notion that recapture is not possible.

Based on the assessed values reported by the five counties in which the Yadkin River Project is located, the total tax value is $140.5 million. The assessed value is divided by the sales assessment ratio for each county to determine the estimated market value. The sales assessment ratio is an estimate of how close assessed values are to market values. The estimated market value for the Yadkin River Project based on these calculations is $176 million.

Compiling all of these data, Fiscal Research anticipates that the cost of acquiring the Yadkin Project would fall somewhere within the range of $24.2 million to over $500 million, with the most likely estimate being something closer to the estimated market value of $176 million which is based on the tax values provided below.

County	**Tax Value of Alcoa Property**	**Sales Assessment Ratio**	**Estimated Market Value**
Stanly	$49,122,910	0.82	$59,905,988
Montgomery	$62,929,298	0.72	$87,401,803
Davidson	$26,567,135	0.99	$26,835,490
Davie	$1,472,349	0.91	$1,617,966
Rowan	$495,697	0.97	$511,028
Total	**$140,587,389**		**$176,272,274**
Note: Tax values are based on all property owned by Alcoa in each county, some of which may not be included in the Yadkin Project.			

[2] Alcoa, *Yadkin Hydroelectric Project FERC No.2197 Application for License*, Volume 1, Exhibit D, 2006. Available online at http://www.alcoa.com/yadkin/en/relicensing/FERC_application.asp.

Cost of Assuming the FERC License
The bill stipulates that the Yadkin Trust can pursue transfer of the license, file an application for a new license, amend the existing license, or take any other actions necessary to become the licensee. Alcoa spent five years working on the license application and the relicensing settlement agreement. They had 23 environmental technical studies conducted and held meetings with various stakeholder groups. In its 2006 License Application, Alcoa stated that preparation of the license application cost approximately $20 million.

Cost of Capital and Other Improvements to the Yadkin Project
Alcoa contends that extensive capital improvements are needed at the Yadkin Project to insure compliance with the Relicensing Settlement Agreement (RSA). New GS 77-156(b) requires that the Trust comply, to the maximum extent practicable, with all terms and conditions of RSA. As of April 24, 2009, Alcoa estimates that such improvements will cost $194.5 million and asserts that these costs would need to be assumed by whomever operates the Project. In the original License Application, Alcoa stated that $130.5 million (2005 dollars) and $1.5 million in annual costs were needed for capital investments.

Lobbyists for Stanly County agree that “major maintenance” may be necessary. They cite an estimate by Dr. Steve Scroggin, a visiting assistant professor of economics at Virginia Tech, that new enhancements may cost $1.5 million annually with $4 million in one-time costs.

The range for capital improvement costs provided by the two parties is quite broad - $4 million in one-time costs and $1.5 million in annual costs compared to $194.5 million one-time and $1.5 million annually – and is most likely not an apples-to-apples comparison. Moreover, it is not clear how much these estimates correspond to the requirements specified in the bill. Further study and independent analysis would be needed for Fiscal Research to be able to provide an estimate of these costs.

Cost of Operating the Yadkin Project
New GS 77-154 thru 77-156 describe the powers and duties of the Yadkin River Trust including producing, distributing, and selling hydroelectric power.

New GS 77-154(b) creates an executive director position to be appointed by the board with a salary fixed by the board. Presumably there will be costs incurred to the State for this position; however the salary is not stipulated, so the costs are unknown at this time. Additionally, new GS 77-154(c) enables the Trust to employ consultants, and new GS 77-154(d) allows the Board to enter into contracts to operate the Yadkin Project. The following provides a range of estimates for the potential operational costs for the Trust.

Alcoa asserts that their annual operating expenses, including salaries and benefits for 32 employees, and depreciation costs are approximately $28.3 million. A breakdown of these expenses for 2005 is provided by Alcoa as Table D.4-1 in its License Application and is as follows:

Cost of Capital (equity and debt)	$8,615,579

Depreciation	$9,083,141
Operation & Maintenance	$9,296,093
FERC Administrative Fee	$466,241
Property Taxes	$849,043

The Yadkin Trust, as a public agency, would not incur the income taxes that Alcoa currently pays of $5.3 million (State and Federal combined) nor the property taxes paid – which were $1.3 million in 2008.

Stanly County in its brief to ERC estimated operating expenses to be $2.5 million annually with an additional $1.5 million annually for enhancements and capital improvements.

Cost of Environmental Site Assessments and Remediation
New GS 77-156 requires that the Yadkin River Trust conduct environmental site assessments and remediation of properties currently or formerly owned by Alcoa in the Yadkin River Basin and other sites at the Badin Work site; remediation is to be done to an unrestricted use level. Fiscal Research does not have an estimate for the cost of such assessments and remediation, but based on other environmental cleanups with significant contamination, costs could potentially be in the multi-million dollar range. Unrestricted use is a high standard that requires extensive cleanup as compared to risk-based remediation which allows for some contamination to remain. It should be noted that the Trust is required to pursue legal action against responsible parties which may defray the costs of cleanup but may bring with it legal expenses.

Costs to the Department of Commerce to Develop a Business Plan
Section 10(g) requires the Department to present a detailed business plan for the operation of the Yadkin River Trust to the Joint Legislative Commission on Governmental Operations and the Joint Legislative Utility Review Committee on or before March 1, 2010. As the Department is already in the process of creating the plan, no additional appropriation will be required for this Section.

Debt Financing
HB 1099 does not authorize the Trust to issue any form of debt. The bill does require the Trust to request the authority to issue revenue bonds from the General Assembly, if the Trust acquires the FERC license.

<u>Revenues</u>
According to Alcoa, the Yadkin Project has a total generating capacity of 215 megawatts of electricity.[3] Alcoa claims that average annual revenue is approximately $43.6 million. Alcoa asserts that annual expenses and depreciation costs are approximately $28.3 million. Additionally, the annual costs associated with the new license would be $1.6 million. Thus, profits before taxes would be approximately $13.7 million.

Lobbyists for Stanly County contend that profits could be $35 million, or more, annually. In its brief to ERC, Stanly County stated that they estimated the Yadkin Project gross annual revenues to

[3] Alcoa website, accessed April 25, 2009, http://www.alcoa.com/yadkin/en/info_page/hydropower.asp.

be at least $40 million with annual costs of about $2.5 million and new enhancements of $1.5 million annually.

Thus, Fiscal Research estimates that annual revenues for the Trust would be between $13.7 million and $35 million.

Use of Revenues
The bill stipulates that the Trust shall first use revenues to operate the Yadkin Project and then to fulfill the duties under GS 77-156. GS 77-156 requires that the Trust remediate environmental contamination, as explained under the "Costs of Environmental Site Assessments and Remediation" section above. The Trust is then to direct proceeds to the Power for Jobs Fund and the Community College System, and any remainder of funds shall be used to fund projects and improve the health of the Yadkin River and River Basin.

Power for Jobs
The bill states that 25% of the net proceeds from the Yadkin River Project's electrical output will go to a "Power for Jobs" fund to be established in the Department of Commerce. The fund will be used to make grants to businesses and nonprofits to create or retain jobs in the Yadkin River Basin. The Department of Commerce currently administers several statewide economic development funds. Administration of the Power for Jobs Fund can be handled within existing resources. No additional appropriation will be required.

Community College System
From the grants made by the Yadkin River Trust to the North Carolina Community College System, the State Board of Community Colleges will allocate funds to the 58 community colleges for instructional equipment. It should be noted that the System has a $40.3 million base budget for equipment, but has an equipment stock valued at $320 million. Current funding will allow average equipment replacement to occur every eight years.

Tax Analysis
The Yadkin River Trust will be exempt from property taxes as a governmental entity. The amount of property taxes paid to local governments for the Yadkin River Project in 2008 was $1,307,885. The Trust would also not incur the income taxes that Alcoa currently pays of $5.3 million (State and Federal combined).

SOURCES OF DATA: Department of Transportation; Department of Environment and Natural Resources; Stanly County Assessor's Office; Davie County Assessor's Office; Davidson County Assessor's Office; Montgomery County Assessor's Office; Lobbyists for Alcoa and APGI; Lobbyists for Stanly County; Documents prepared by Stanly County for the Environmental Review Commission and Documents prepared by APGI for the Environmental Review Commission available online at http://www.ncleg.net/gascripts/DocumentSites/browseDocSite.asp?nID=12&sFolderName=\Alcoa%20-%20Stanley%20County%20-%20FERC%20Re-licensing; Alcoa Licensing and Relicensing Documents available online at http://www.alcoa.com/yadkin/en/info_page/relicensing_overview.asp.

TECHNICAL CONSIDERATIONS: None

FISCAL RESEARCH DIVISION: (919) 733-4910

PREPARED BY: Kristin Walker, Rodney Bizzell, Lanier McRee, Kristine Leggett, Jim Klingler, Richard Bostic, Bob Weiss

APPROVED BY: Marilyn Chism, Director
Fiscal Research Division

DATE: August 7, 2009

Official Fiscal Research Division Publication

Signed Copy Located in the NCGA Principal Clerk's Offices