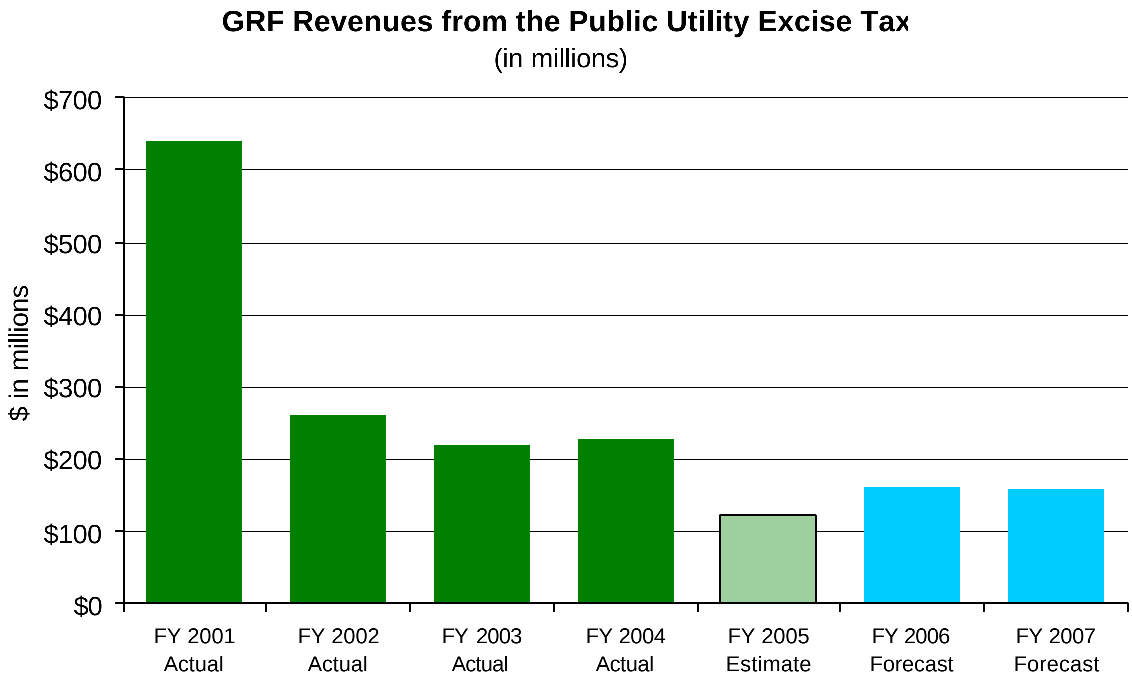
Public Utility Excise Tax



	FY 2001 Actual	FY 2002 Actual	FY 2003 Actual	FY 2004 Actual	FY 2005 Estimate	FY 2006 Forecast	FY 2007 Forecast
Revenue	$640.5	$260.1	$218.7	$226.4	$123.0	$160.0	$158.0
Growth	-0.2%	-59.4%	-15.9%	3.6%	-45.7%	30.1%	-1.3%

The public utility excise tax — also known as the gross receipts tax — is a tax on the intrastate revenues of public utilities. The tax is levied on natural gas utilities, pipeline companies, heating companies, waterworks, and water transportation companies. All companies subject to the tax pay a tax of 4.75% of gross receipts except pipeline companies, who pay a tax of 6.75% of gross receipts.

The significant fall in revenue from the tax in FY 2002 is attributable to the removal of electric companies from the tax by Am. Sub. S.B. 3 of the 123rd General Assembly. The tax receipts lost because of dropping electric companies from this tax were intended to be replaced by corporate franchise tax payments and by payments under the newly created kilowatt-hour tax, which was created by S.B. 3. Similarly, the anticipated fall in revenue in FY 2005 is attributable to removal of telephone companies from the tax by Am. Sub. H.B. 95 of the 125th General Assembly. This reduction in tax receipts was intended to be replaced by corporate franchise tax payments and by payments under the sales tax. The significant increase in revenue forecast for FY 2006 is due primarily to the assumed return to the statutory distribution of revenue under the tax. The freeze in local government funds' shares of the tax provided by H.B. 95 froze payments to the local government funds from this tax at a level when both electric companies and telephone companies were paying the tax. Therefore, returning the tax to its statutory formula would lead to a significant increase in the GRF share of tax revenues; an estimated increase of over $28 million in FY 2006.

With the departure of electric companies and telephone companies, natural gas utilities will contribute approximately 97% of the revenue collected under this tax. Because all other utility companies will account for under 3% of receipts under the tax, the discussion that follows will be restricted to the assumptions underlying the forecast for the receipts from natural gas companies.

Natural gas utilities paid $149.8 million under the tax in FY 2004. The tax is paid by utilities, not marketers. Nonutility companies that sell gas on a retail basis under the Choice Program do not pay the tax, but they are supposed to collect sales tax on their sales. Most industrial customers are in practice exempt from the sales tax due to the exemption for direct use in manufacturing. Participation in the Choice Program has fallen somewhat recently; as of November 2004, 37.0% of residential customers statewide were enrolled in a Choice Program compared with 42.9% in December 2003. Similarly, 39.1% of commercial customers were enrolled in a Choice Program in November 2004, down slightly from 42.3% in December 2003. Thus the share of natural gas residential customers still subject to the tax (i.e., those not enrolled in a Choice Program) in November was 110.4% of the share subject to the tax in December 2003, and the corresponding share of commercial customers was 105.6%. Taking an appropriate weighted average of these shares, the share of natural gas customers subject to the tax increased by approximately 8.8% during this period. This implies that tax revenues attributable to natural gas companies will be about this percentage higher in FY 2005 than they would have been with no change in Choice Program participation.

Officials with the Public Utility Commission of Ohio indicate that the recent reduction in Choice Program participation is likely due to specific circumstances involving certain suppliers and government aggregators. They believe that the number of suppliers is sufficient to expect that the reduction in participation does not represent the beginning of a trend. Therefore, participation in the Choice Program is projected to resume its trend prior to the recent unusual circumstances, i.e., to begin to increase slightly each year. The forecast assumes the Choice Program participation increases by 2% in calendar year 2005 (affecting FY 2006 revenues) and by an additional 2% in 2006 (affecting FY 2007 revenues). While LSC economists believe that enrollment increases in Choice Programs are the most likely outcome over the next two years, unexpected news could swing customers away from them, or accelerate the recent enrollment trend, in a dramatic fashion. That would change receipts for this tax, but it should be balanced by changes in sales tax receipts in the opposite direction.

Even more than the effects of enrollment in a Choice Program, the receipts from the tax depend on changes in the market price of natural gas and the volume of gas used. Forecasts of these changes are taken from the Global Insight (formerly DRI-WEFA) economic forecast for the U.S. published in January 2005. The following table presents the Global Insight forecasts of natural gas demand (volume) and price changes nationwide between the first quarter of the preceding calendar year to the first quarter of the year shown in the table:[9]

Global Insight forecast of changes in U.S. natural gas prices, volumes used		
Year	**Price**	**Volume**
2005	12.8%	-1.1%
2006	-3.5%	-0.1%
2007	-5.4%	0.4%

[9] The U.S. Energy Information Administration (EIA) forecasts that natural gas prices will rise by about 3% from 2005 to 2006, and that natural gas demand will increase by 3.0% in 2005 and by an additional 2.1% in 2006. Therefore, basing the revenue forecast on the Global Insight economic forecast may be somewhat conservative, in the sense of producing a slightly lower revenue forecast than would be produced by basing it on the EIA forecast of energy demand and prices. One reason for preferring the Global Insight forecast is that both demand and prices are forecast on a quarterly basis rather than an annual basis.