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"Maryland's Experience with the Bay Restoration Fee"

Chairman Johnson, and honorable members of the Committee, thank you for the opportunity to share Maryland's experience with the Bay Restoration Fund. In this testimony I am providing information requested by your staff regarding Maryland's experience with the Bay Restoration Fund that I hope will be of value in your deliberations regarding creation of a federal fund to address the critical national issue of restoring our nation's water and wastewater infrastructure.

Maryland has a very significant water and wastewater infrastructure need, estimated to be approximately $14 billion total. Maryland's federal and state water and wastewater capital funding is currently $130 million per year. If we hope to meet the projected need over the next 20 years, we will have to identify additional revenue to fill an annual funding gap of over $500 million. Maryland's Bay Restoration Fund covers a small part of this need -- that related to upgrading the State's 67 largest sewage treatment plants to achieve Enhanced Nutrient Removal -- but between now and 2029 (the time needed to pay back the revenue bonds issued) the fund is fully committed and will meet only about $1 billion of the total $14 billion estimated need. The Bay Restoration Fund is an important part of Maryland's solution, but it is not the whole solution. Maryland depends upon the Clean Water State Revolving Fund (CWSRF) and Drinking Water State Revolving Fund (DWSRF) and **strongly** supports President Obama's (and many of your) efforts to strengthen these critical federal programs.

How did we overcome political and other obstacles in order to get the Bay Restoration Fund bill passed?

The majority of Maryland's citizens have always been very concerned and interested in the restoration of Chesapeake Bay and Maryland has a long history of strong support for State programs to restore the Bay. In 1983 the first Chesapeake Bay Agreement between the federal government, Maryland, Virginia, Pennsylvania and the District of Columbia was signed. In 1984, former Governor Hughes and the State legislature created a comprehensive legislative package to initiate the Bay restoration, including establishing a State cost-share funding program for wastewater treatment plant upgrades to remove nutrients, promoting a relatively new technology known as Biological Nutrient Removal (BNR). In 2000, former Governor Glendening had signed the Chesapeake 2000 Agreement with the federal government that increased Maryland's Bay commitments further and established a restoration deadline of 2010.

By 2004, MD had achieved significant levels of nutrient reduction at its sewage plants (52% nitrogen removal and 62% phosphorus removal), but it was clear to everyone that significant additional steps would be needed to meet the Bay restoration goals. As one of the largest and most cost-effectively controlled sources, Maryland's sewage plants once again became the focus. In Maryland's 2004 legislative session, former Governor Robert L. Ehrlich, Jr. introduced legislation creating the Bay Restoration Fund, which is financed by a $2.50 monthly surcharge on wastewater bills. The Bay Restoration Fund legislation created a revenue stream to fund up to 100% of the cost of upgrades to existing BNR plants to achieve Enhanced Nutrient Removal (ENR).

When it was initially proposed it was immediately dubbed "the flush tax" by the local press, but in reality it was specifically designed by Governor Ehrlich to be a user fee. As the first Republican governor in Maryland in 40 years, and someone who had been labeled as being unsympathetic to environmental issues, the proposed legislation took the Democratically controlled Maryland House and Senate by surprise. However, given the strong public support for Bay restoration, the legislature quickly came to a position of nearly full support for the Governor's legislation. In addition, the Democratic leadership of the legislature amended the bill to include a similar user fee for owners of onsite sewage disposal systems (primarily septic systems) that supports a grant program for voluntary onsite system upgrades to remove nitrogen homeowners and businesses by that are not served by public sewer systems.

The legislation clearly built upon Maryland's previous Bay restoration efforts and in testimony and in the press the Governor and the legislature emphasized the fact that that the users were paying a reasonable fee to mitigate their personal impacts on the Bay. With over 20 years of emphasis on Bay restoration, education and outreach, there was general public understanding of the need and strong support from the environmental community. The business and agricultural communities were strong supporters of Governor Ehrlich and he was able to marshal their support as well. The bill passed with little significant opposition.

How is the fee structured?

The Bay Restoration fee is paid by all users of municipal waterwater treatment facilities, all owners of private onsite sewage treatment systems and by all commercial and industrial facilities that discharge nutrients to the waters of the State. The fee is structured as a flat rate ($2.50 per month or $30 per year) for residential wastewater treatment system users and is paid as a surcharge on the water or sewer bill. For private onsite systems, the fee is paid annually directly to the County government. For commercial and industrial users, the fee is a multiple of the residential rate based on the amount of sewage discharged. For example, a 500 room hotel that uses 15,000 gallons per day, which is 60 times the amount of water used by the typical residence (250 gallons per day), would pay $150 per month. The fee is capped for very large water users (mostly industrial processes) and discharges that do not contain nutrient are exempt (e.g. cooling water). The local government or other water/sewer billing authority may retain

up to 3% of the annual surcharge to cover administrative expenses associated with the billing process. The State agency responsible for administering the grant program and reviewing and approving the construction of the upgraded facilities retains 1.5%. The legislation also requires that the Governor appoint an independent advisory committee to oversee the Fund and provide an annual report to the Governor and the legislature.

How is it being used?

The revenue the Bay Restoration fee is paid into two different dedicated funds, one for the municipal wastewater user's fee and one for the private onsite sewage system owner's fee. Both are special, non-lapsing funds that may only be used for specified purposes. The Wastewater users fund is used to provide grants to local governments and sanitary commissions to fund up to 100% of the cost of upgrading treatment plants that are already achieving advanced BNR wastewater treatment levels to achieve ENR levels of nitrogen and phosphorus removal. If a plant to be upgraded is not yet achieving BNR levels of treatment, the grant only pays for differential between a BNR upgrade and an ENR upgrade. The legislation mandates that the funds be used to upgrade the facilities that will result in the most cost-effective nutrient reduction.

The onsite sewage system user's fee is split; 60% is used to provide grants to owners to upgrade their onsite systems to remove nitrogen and 40% is directed into the Maryland Department of Agriculture's cover crop program that provides financial support to farmers that plant winter cover crops on their fields. Cover crops are eligible for funding since they are a much more cost-effective means of controlling nutrient losses from cropland to groundwater in rural areas of the state where onsite systems are used. Onsite systems must be upgraded with technology approved by the Maryland Department of the Environment that meets certain nutrient removal requirements.

To date, the wastewater user's fee has generated over $219 million and is currently projected to continue to generate over $55 million per year. The dedicated revenue stream is supporting the issuance of 20-year revenue bonds that will raise nearly $1 billion needed to upgrade the State's 67 largest sewage treatment plants. The investment in these upgrades will reduce nitrogen loading the Bay by an additional 7.5 million pounds per year, which is roughly 1/3 of the total nitrogen reduction needed to meet Maryland's commitment for the Chesapeake Bay restoration.

The onsite sewage system owner's fee has generated over $50 million and is expected to continue to generate over $14 million per year. The funding will support upgrades of another 650 to 700 onsite sewage disposal systems each year and provide $5 - $6 million per year to supplement the State's cover crop program, which together will reduce nutrient loading by over 1.5 million pounds per year.

Observations based on Maryland's experience regarding the proposed Clean Water Trust Fund

The public support for the Bay Restoration Fund is based on several key factors. First, the long history of the Bay restoration effort in Maryland over the past two decades prior to the proposal of the 2004 Bay restoration fee legislation resulted in public understanding and support for the Bay restoration effort in general. Second, the source of the fee, a surcharge on wastewater bills, is understood to be directly related to the impact and the solution – wastewater treatment plant upgrades. Third, the fee is reasonable and is equitably distributed since larger users are assessed a higher fee. Finally, the fee is capped, so that no single user pays a disproportionate share.

The potential funding options discussed in the General Accounting Office report range from a fee based on water use, similar to the Bay restoration fee, to a general corporate income tax. Based on the Maryland experience, the more closely the fee or tax is associated with the problem, the better it will be received. The water use fee, industrial discharge fee and excise taxes on flushable products, water appliances and fixtures and fertilizers and pesticides seem most closely related. Also related, although perhaps not as clearly understood by the public, are the excise taxes on beverages and pharmaceuticals. Least acceptable are likely to be the corporate income tax and other more general taxes.

Finally, the fee or taxes must be perceived as fair. Maryland's fee is distributed across all sectors that contribute to the wastewater problem and is scaled to the level of impact. This can be most readily accomplished with the fee based on wastewater use. Excise taxes that necessarily focus on one or even several sectors are often perceived as unfairly singling out those sectors.