Economic Impact Statement

Office of Legislative Oversight

Expedited BILL 50-20 — Landlord-Tenant Relations – Fire Safety – Removal of Mercury Service Regulators

SUMMARY

The Office of Legislative Oversight (OLO) believes that enacting Expedited Bill 50-20 would potentially increase costs to private organizations and residents subject to any increase in gas utility rates related to the replacement of mercury service regulators. OLO anticipates that the bill could have a negative economic impact on the County.

BACKGROUND

The purpose of Expedited Bill 50-20 is to improve fire safety by promoting "the immediate replacement of indoor mercury service regulators with safer, more modern regulators."[1] If enacted, Expedited Bill 50-20 would change the law regarding landlord obligations in several ways. Landlords would be required to determine whether there are any mercury service regulators (MSRs) on the premises of rental properties they lease.[2] If they identify any MSRs, landlords would be required to contact the gas utility company to schedule the immediate removal of the regulators.[3] Landlords would also be required to provide notifications to tenants during the process of detection and removal of MSRs.[4] Expedited Bill 50-20 would assign the Department of Housing and Community Affairs (DHCA) with enforcing the new regulations, and require DHCA to maintain a public database that includes information on the status of the detection and removal of MSRs and any enforcement actions.[5]

Expedited Bill 50-20 would apply to all rental properties in the County that are subject to the Department of Housing and Community Affairs (DHCA) enforcement. The scope of the law would exclude properties within municipalities that have not opted into Chapter 29 of the Montgomery County Code. DHCA personnel estimate that approximately 690 rental properties and 70,000 units were subject to the department's enforcement in 2017. These figures represent the best estimate of the number of rental properties that would be impacted by the expedited bill.

The requirements set forth in Expedited Bill 50-20 would complement efforts under way to replace MSRs throughout the state. In 2002, Washington Gas and Light Company (WGL) committed to replacing all MSRs in its Maryland service area within 10 years.[6] The Maryland Public Service Commission (hereinafter "the commission"), the entity that regulates gas utilities operating in the state, has *twice* approved the company's requests to increase rates for utility services to recover costs associated with the removal of MSRs.[7] However, the company has not completed the removal of MSRs. In its recent

[1] Christine Wellons to Montgomery County Council, Memorandum, December 3, 2020, https://apps.montgomerycountymd.gov/ccllims/DownloadFilePage?FileName=2688_1_12107_Bill_50-2020_Introduction_20201208.pdf.
[2] Montgomery County Council, Expedited Bill 50-20, Landlord-Tenant Relations – Fire Safety – Removal of Mercury Service Regulators, Introduced on December 8, 2020, 2, https://apps.montgomerycountymd.gov/ccllims/DownloadFilePage?FileName=2688_1_12107_Bill_50-2020_Introduction_20201208.pdf.
[3] Ibid, 3.
[4] Ibid, 2-3.
[5] Ibid, 3-4.
[6] Initial Brief of the Maryland Office of People's Council, Case No. 9622, Filed on October 28, 2020, https://www.psc.state.md.us/search-results/?q=9622&x.x=23&x.y=15&search=all&search=case.
[7] Ibid.

decision to fine Washington Gas in a case relating to the 2016 gas explosion at the Flower Branch apartments in Silver Spring, the commission decided that "the MSR Replacement Program as outlined in the 'Revised Stipulation and Settlement' in Case No. 8920 constituted a *binding commitment* by WGL to remove all indoor MSRs within 10 years" (emphasis added).[8] In addition, the commission approved WGL's new replacement program with modifications and directed the company to:

- "maintain accounts of all capital and operating expenses, including any incremental costs related to the program;"
- "include these expenses in its annual status report;" and
- "record and maintain a list of all requests to remove an MSR from residential properties."

To recover any costs associated with the removal of MSRs, WGL would need to apply and attain approval from the commission to increase base rates. In its ruling, the commission did not "address prudency or recovery of costs associated with this new MSR replacement program since projected costs are not available at this time."

METHODOLOGIES, ASSUMPTIONS, AND UNCERTAINTIES

The economic impacts associated with replacing MSRs would occur through two primary channels:

- **Change to the utility base rate for customers in the service territories of utility companies.** A future base rate adjustment would be the primary channel through which the costs incurred in the removal of MSRs would be passed from gas utilities to private organizations and residents in the County.
- **Contracts awarded to third-party companies for the removal of MSRs.**[9] Economic benefits would be channeled to local businesses that are awarded contracts to remove MSRs.

At this juncture, it is unknown whether the MSR removal costs will be recovered through an upward adjustment to the base rate. The Maryland Office of the People's Council (OPC) and the Apartment and Office Building Association of Metropolitan Washington (AOBA) have argued that ratepayers should not bear the cost of removing MSRs.[10] If WGL (or any other utility company) applies for a rate change in the future, it would be up to the discretion of the commission on whether to approve the request.

In addition to the occurrence of a rate change, the magnitude of any change to the rate cannot be estimated. A representative from WGL informed OLO that the cost of removing an MSR is approximately $1,800. (Note that this amount is significantly greater than the $200 per unit replacement cost the company has reportedly cited previously.[11]) While

[8] Order No. 89680, In the Matter of an Investigation of Washington Gas & Light Company Regarding a Building Explosion and Fire in Silver Spring, Maryland, Case No. 9622, Issued on August 10, 2016, December 18, 2020, https://www.psc.state.md.us/wp-content/uploads/Order-No.-89680-Case-No.-9622-WGL-FB-Investigation-Order-Assessing-Civil-Penalty.pdf

[9] A representative from WGL informed OLO that the company would contract with third-party vendors for the removal of MSRs. These entities would be the primary beneficiaries of the MSR Replacement Program.

[10] Order No. 89680; Initial Brief of the Maryland Office of People's Council.

[11] The Washington Post recently reported that "[w]hile seeking a rate increase in 2003, the gas provider said it would replace all 66,793 of its indoor mercury gas regulators over the next decade to address age and environmental concerns. The utility said it would deploy a staff of seven to replace more than 6,000 regulators a year for 10 years at a cost of about $200 per regulator." Steve Thompson, "Washington Gas fined $750,000 in case connected to deadly 2016 explosion," December 22, 2020, https://www.washingtonpost.com/local/md-politics/washington-gas-fine-flower-branch/2020/12/21/e502b034-43cb-11eb-a277-49a6d1f9dff1_story.html.

WGL states that no more than 10 percent of its customers are likely to have MSRs,[12] the company does not know the total number of remaining MSRs in the County or state.[13] The company is conducting a survey to identify the remaining ones.[14] Moreover, the commission has already approved two rate increases for WGL to recover expenses associated with its MSR Removal Program. If the commission were to approve a rate increase, the total MSR removal costs and amount collected would likely influence the magnitude of any rate change.

Despite these uncertainties, OLO uses available information to estimate the total cost of replacing MSRs in the County. It is important to emphasize that these estimates are not forecasts. They are instead intended to illustrate the general magnitude of MSR replacement costs in the County. Representatives from WGL have stated that the total costs of removing MSRs in the County and state will not be known until after the survey is complete. The estimates are based on the following assumptions:

- Rental properties will have between one and two MSRs;[15] and
- The per unit cost of replacing MSRs is $1,800.

Figure 1 estimates the cost of replacing MSRs in up to 25% of rental properties affected by Expedited Bill 50-20. The cost of replacing MSRs at or below 10% of the rental properties – WGL's upper-bound estimate – may fall short of $500,000.

Importantly, Expedited Bill 50-20 would not constitute the primary cause of the costs WGL incurs from replacing MSRs. Given that the commission determined that WGL's MSR Replacement Program constitutes a binding commitment, the removal of MSRs on rental properties in the County that receive gas service from WGL would occur in the absence of Expedited Bill 50-20. However, OLO believes it is possible that the requirements set forth in the bill (requiring landlords to detect MSRs and schedule for their immediate removal, and DHCA to maintain a database on the status of MSR detection and removal) could potentially have two results:

- A more complete accounting of all the MSRs in the County; and/or
- Expediting the removal of MSRs.

Expedited Bill 50-20 would be responsible for only the costs associated with these potential outcomes, not the total cost of removing MSRs within WGL's service territory in the County.

In terms of other gas utilities operating in the County, the bill may be responsible for the entire costs of replacing MSRs. WGL appears to be the only gas utility that has an MSR replacement program underway. Expedited Bill 50-20 may compel other utility companies to replace MSRs in the County, thereby increasing the number of replaced MSRs that would otherwise not have occurred in the absence of the bill's enactment. However, OLO cannot estimate the number of MSRs that would fall into this category nor the total cost of replacing them, because we have been unable to attain information on the percentage of the approximately 690 rental properties under the enforcement of DHCA that fall within the respective gas utilities' service territories. Nevertheless, it is OLO's understanding that the majority of private organizations and residents who would be affected by Expedited Bill 50-20 are WGL customers.

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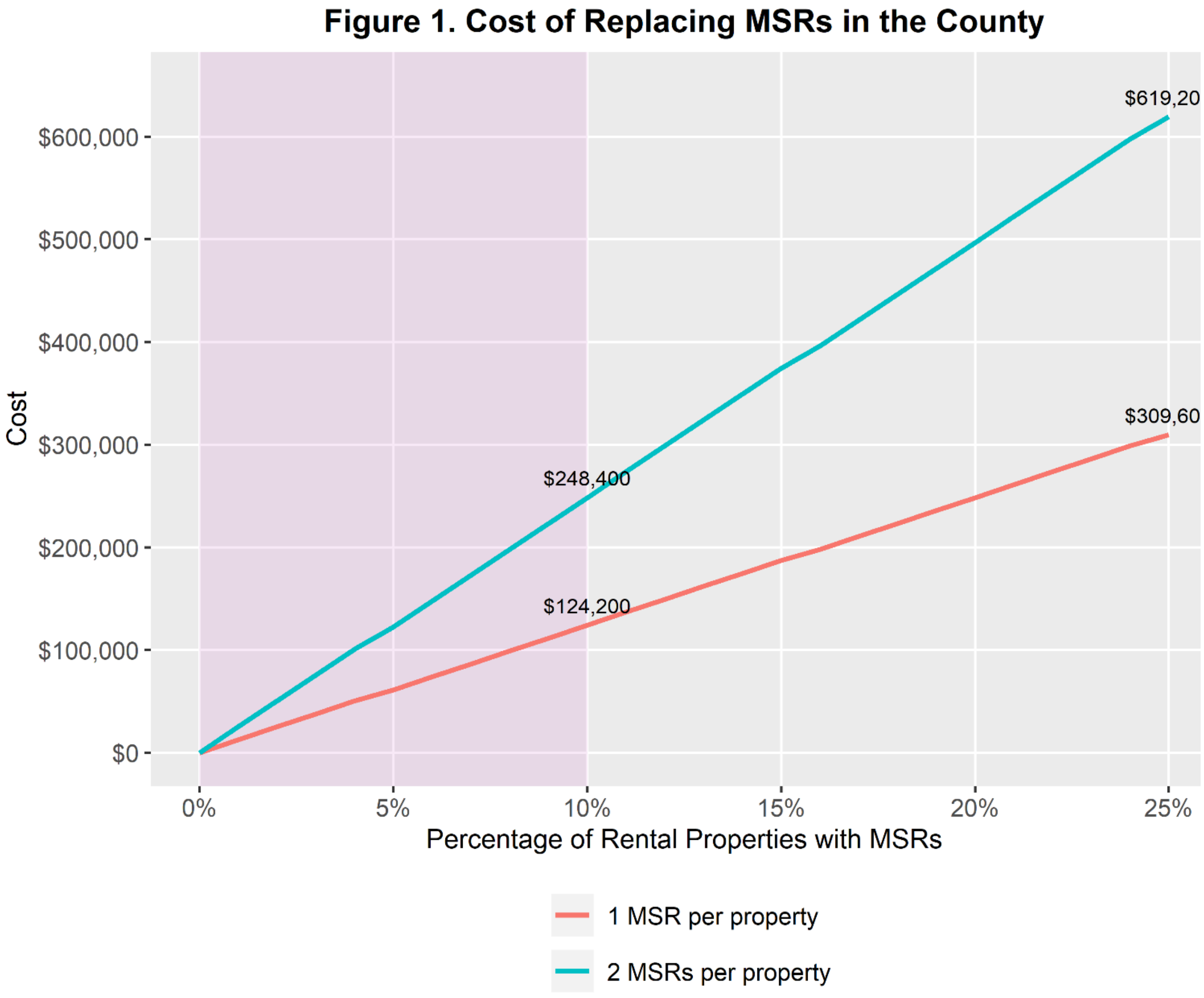
[12] Washingtongas.com, Information about Mercury Service Regulators, Washington Gas, https://www.washingtongas.com/media-center/customer-advisory-mercury-regulators.

[13] Order No. 89680.

[14] Ibid.

[15] In our correspondence with a representative from WGL, OLO was informed that multi-family rental properties may have up to two MSRs. We were unable to attain any more information that would allow us to make a more precise estimate of the average number of MSRs per rental property.

Ultimately, due to WGL's market share and the MRS Replacement Program that is underway, OLO assumes that the bill would be responsible for a minority portion of any increase in the base rate due to MSR replacement costs.



VARIABLES

The primary variables that would affect the economic impacts of Expedited Bill 50-20 are:

- Total amount already collected by WGL for MSR detection and removal;
- Number of remaining MSRs in the County and state;
- Per unit cost of replacing MSRs;
- Percentage of affected rental properties within WGL's service territory;
- Total amount of contracts awarded to local businesses for the removal of MSRs;
- Change to base rates to recover MSR removal costs; and
- Percentage of base rate hikes passed on by landlords to tenants.

IMPACTS

WORKFORCE ▪ TAXATION POLICY ▪ PROPERTY VALUES ▪ INCOMES ▪ OPERATING COSTS ▪ PRIVATE SECTOR CAPITAL INVESTMENT ▪ ECONOMIC DEVELOPMENT ▪ COMPETITIVENESS

Businesses, Non-Profits, Other Private Organizations

Expedited Bill 50-20 would have direct economic impacts on landlords of the approximately 690 rental properties subject to DHCA enforcement, and any companies that receive contracts for the removal of MSRs.[16] The bill would require owners of the approximately 690 rental properties subject to DHCA enforcement to determine if there are MSRs on the premises of their properties. However, OLO does not anticipate that there would be significant costs associated with detection. WGL's website provides instructions and support on how to detect MSRS, and states that MSRs "can be identified easily."[17] If this is the case, the direct negative economic impacts of Expedited Bill 50-20 on landlords would instead occur through costs associated with notifying tenants of the status of detection and removal of MSRs (e.g., paper, envelopes, postage). OLO anticipates that these costs would be minimal. These direct costs, as well as any potential indirect costs (see below), could be offset by passing them onto tenants in the forms of higher rents.

Local businesses may also experience direct economic benefits from Expedited Bill 50-20. WGL plans to contract with companies for the removal of MSRs. It is possible that companies based in the County may receive contracts for the removal of MSRs in the County and state. Local businesses awarded contracts would experience a net increase in business incomes.

Furthermore, Expedited Bill 50-20 may result in negative *indirect* impacts on private organizations in the County. These impacts would be mediated by the commission.[18] As previously stated, the commission may approve requests by WGL and/or other utilities to increase base rates to recover costs associated with replacing MSRs, a portion of which may be attributable to the bill. Such an adjustment would apply to all customers subject to the rate schedule. Any upward

[16] For the Council's priority indicators, see Montgomery County Council, Bill 10-19 Legislative Branch – Economic Impact Statements – Amendments, Enacted on July 30, 2019, Montgomery County, Maryland, 3.
[17] Washingtongas.com, Information about Mercury Service Regulators.
[18] Here, I use "indirect impacts" to refer to the effects of a change in law on private organizations/residents that are mediated or transmitted through another entity. This definition is distinct from the one used in Input-Output analysis, in which an "indirect impact" is defined as a "[c]hange in economic activity resulting from the subsequent rounds of inputs purchased by industries affected by a final-demand change." See *RIMS II: An Essential Tool for Regional Developers and Planners*, U.S. Bureau of Economic Analysis, December 2003.

adjustment to the base rate for gas utilities would increase operating costs for the affected private organizations, thereby reducing their net operating income.

OLO does not expect Expedited Bill 50-20 to have impacts on the Council's other priority indicators, particularly taxation policy, property values, private sector capital investment, economic development, or competitiveness.

Residents

Expedited Bill 50-20 could result in direct and indirect economic impacts to residents. In terms of direct impacts, owners and employees of local businesses that are contracted to replace MSRs could experience additional earnings. All residents subject to an increase in utility rates designed to recover MSR replacement costs would experience a net increase in household expenses. Moreover, to the extent that landlords pass on costs caused by the bill to their tenants, these renter households would also experience a net increase in expenses.

QUESTIONS FOR CONSIDERATION

OLO has recently produced economic impact statements for three bills (Expedited Bill 50-20, Bill 51-20, and Bill 52-20) related to rental housing and landlord responsibilities. All three are likely to have a negative economic impact on landlords. Should the Council desire more economic analysis, OLO suggests conducting an examination of the aggregate economic impact of these bills.

WORKS CITED

Christine Wellons to Montgomery County Council. Memorandum. December 3, 2020. https://apps.montgomerycountymd.gov/ccllims/DownloadFilePage?FileName=2688_1_12107_Bill_50-2020_Introduction_20201208.pdf.

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CAVEATS

Two caveats to the economic analysis performed here should be noted. First, predicting the economic impacts of legislation is a challenging analytical endeavor due to data limitations, the multitude of causes of economic outcomes, economic shocks, uncertainty, and other factors. Second, the analysis performed here is intended to *inform* the legislative process, not determine whether the Council should enact legislation. Thus, any conclusion made in this statement does not represent OLO's endorsement of, or objection to, the bill under consideration.

CONTRIBUTIONS

Stephen Roblin (OLO) drafted this economic impact statement.